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Note

Securities Law: Implied Causes of Action Under Section 14(e) of the Williams Act

I. INTRODUCTION

Section 14(e) of the Securities and Exchange Act of 1934 (1934 Act) prohibits a variety of fraudulent practices "in connection with any tender offer."¹ In passing this legislation, Congress did not explicitly give target company shareholders the right to sue under section 14(e). The federal courts and the Securities and Exchange Commission (SEC) have consistently struggled to determine whether Congress intended to provide a private cause of action for target shareholders under section 14(e) and, if it did so intend, the circumstances under which that cause of action arises.

Although most lower federal courts and commentators agree that a private cause of action is implied under section 14(e),² they disagree as to the action's scope. Two distinct approaches to this latter problem have developed. Most federal courts have thus far allowed target shareholders to sue under section 14(e) only to prevent or offset damages that they may incur in deciding whether to tender their shares.³ The SEC⁴

1. 15 U.S.C. § 78n(e) (1976). Congress originally enacted section 14(e) as part of the Williams Act, Pub. L. No. 90-439, 82 Stat. 454 (1968) (codified as amended at 15 U.S.C. §§ 78m(d)-(e), n(d)-(f) (1976)).

A conventional tender offer "normally consists of a bid by an individual or group to buy shares of a company—usually at a price above the current market price." S. REP. NO. 550, 90th Cong., 1st Sess. 2 (1967) [hereinafter cited as S. REP.]; H.R. REP. NO. 1711, 90th Cong., 2nd Sess. 2 [hereinafter cited as H.R. REP.], reprinted in 1968 U.S. CODE CONG. & AD. NEWS 2811, 2811. Courts have also recognized that unconventional means of carrying out a tender offer exist. See generally E. ARANOW, H. EINHORN & G. BERLSTEIN, DEVELOPMENTS IN TENDER OFFERS FOR CORPORATE CONTROL 1-34 (1977); Note, *The Developing Meaning of "Tender Offer" Under the Securities Exchange Act of 1934*, 86 HARV. L. REV. 1250 (1973).

2. See *infra* notes 59-68 and accompanying text.

3. See *infra* text accompanying notes 59-68.

4. Brief of the SEC, *Amicus Curiae* at 9-22, *Panther v. Marshall Field & Co.*, 646 F.2d 271 (7th Cir.), cert. denied, 102 S. Ct. 658 (1981); SEC *Amicus* Brief, *Levine v. Seilon, Inc.*, 439 F.2d 328 (2d Cir. 1971), reprinted in 85 SEC. REG. & L. REP. (BNA) E-1, E-2 to E-4 (1971).

and some courts⁵ would recognize not only these actions, but would also give shareholders the right to sue to prevent or offset damages that they may incur in deciding whether to sell their shares on the market before the tender offer takes effect.

This Note begins by reviewing why Congress enacted section 14(e). It then analyzes the Supreme Court's general reluctance to recognize implied causes of action, and suggests that the Court's reservations do not apply to shareholder actions under 14(e) based upon shareholder decisions whether to tender their shares. The Note continues by suggesting that there are also sound reasons to imply a cause of action for shareholder actions based on shareholder decisions whether to sell their shares before the tender offer takes effect. Finally, assuming the validity of these implied causes of action, the Note advocates a rule of law defining when to begin holding the target company responsible for pre-tender offer misrepresentations.

II. HISTORICAL AND LEGISLATIVE DEVELOPMENT OF FEDERAL TENDER OFFER CONTROLS

In the 1960's and 1970's, the use of the cash tender offer to acquire control over a target company became widespread.⁶ The tender offer grew in popularity because, unlike mergers, proxy contests, or exchange offers, tender offers were not regulated.⁷ Takeover bidders could, therefore, use surprise tactics to their advantage in forcing quick decisions by shareholders

5. *E.g.*, *Berman v. Gerber Prods. Co.*, 454 F. Supp. 1310, 1325 (W.D. Mich. 1978). For an analysis of this view, see *infra* text accompanying notes 126-72.

6. The aggregate of all the cash tender offers made in 1960 was less than \$200,000,000. By 1965, that total was almost \$1,000,000,000, thus exceeding stock exchange offers, which amounted to \$500,000,000 in both 1960 and 1965. *Full Disclosure of Corporate Equity Ownership and in Corporate Takeover Bids: Hearings on S. 510 Before the Subcomm. on Securities of the Senate Comm. on Banking and Currency*, 90th Cong., 1st Sess. 17 (1967) (statement of Manuel F. Cohen, Chairman, SEC) [hereinafter cited as *Sen. Hearings*]. The number of tender offers increased drastically in the 1960's and 1970's. S. REP., *supra* note 1, at 2; H.R. REP., *supra* note 1, at 2, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2812; E. ARANOW, H. EINHORN & G. BERLSTEIN, *supra* note 1, at vi; Hayes & Taussig, *Tactics of Cash Takeover Bids—For Bidders, Incumbent Managements & Shareholders*, HARV. BUS. REV., Mar.-Apr. 1967, at 135, 136-37. For a breakdown of tender offers for the years 1956-79, see Austin, *Tender Offer Update: 1978-79*, MERGERS & ACQUISITIONS, Summer 1980, at 13, 15.

7. Federal law requires companies making proxy challenges or stock exchange offers to make full disclosure of their intentions before acting to acquire another corporation. For the law governing proxy challenges, see Securities and Exchange Act of 1934, § 14(a), 15 U.S.C. § 78n(a) (1976); 17 C.F.R. §§ 240.14a-1 to .14a-103 (1981). The Securities Act of 1933, §§ 5-8, 10, 15 U.S.C. §§ 77e-h, j (1976), governs stock exchange offers. This Act covers these offers because it

and in thwarting defensive responses by target management.⁸ The cash offer was also easier and less expensive⁹ to implement than a proxy contest.

In these early cash tender battles, offerors often subjected shareholders to risks beyond the shareholders' control. In deciding how to respond to a tender offer, shareholders not only faced time pressures, but also could not obtain information about the managerial policies the offeror would implement upon acquiring the target company.¹⁰ Securities investors thus never knew whether their best interests lay in retaining their securities, tendering them to the offeror, or selling them in the open market.¹¹

Attempts to regulate cash tender offers under existing legislation were unsuccessful. Injured parties could not obtain relief under rule 10b-5,¹² which prohibits fraudulent practices and statements "in connection with the purchase or sale of any security," because it did not place bidders under a duty to disclose their intentions.¹³ In response to the deteriorating situation, Congress amended the 1934 Act in 1968.¹⁴ The legislation, introduced by Senator Williams, was "designed to require

treats an exchange of stock as an issuance of securities. See *United States v. Riedel*, 126 F.2d 81, 83 (7th Cir. 1942).

8. Before 1968, when Congress passed the Williams Act, offerors could force shareholders to act within very limited time periods. Easterbrook & Fischel, *The Proper Role of a Target's Management in Responding to a Tender Offer*, 94 HARV. L. REV. 1161, 1162 n.6 (1981). Offerors could also specify that shareholders' tenders were irrevocable. *Id.*

9. Fleischer & Mundheim, *Corporate Acquisition by Tender Offer*, 115 U. PA. L. REV. 317, 320-21 (1967). One study indicated that the costs of a proxy contest are three times that of a cash tender offer. Wall St. J., Feb. 11, 1966, at 1, col. 6. The study treated the money that the bidder spends in buying target company stock as an investment, rather than as an expense of the offer. *Id.*

10. The discussion in Congress that preceded the passage of section 14(e) pointed out the shareholder's lack of information. "At present, the law does not even require that [a takeover bidder] disclose his identity, the source of his funds, who his associates are, or what he intends to do if he gains control of the corporation." S. REP., *supra* note 1, at 2; H.R. REP., *supra* note 1, at 2-3, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2812.

11. See *id.*

12. 17 C.F.R. § 240.10b-5 (1981). The SEC enacted the regulation under the authority of section 10(b) of the 1934 Act. 15 U.S.C. § 78j(b) (1976).

13. Rule 10b-5 mandates disclosure of one's intentions only in insider trading situations. See *Chiarella v. United States*, 445 U.S. 222, 230, 235 (1980). A fiduciary relationship, giving rise to the duty to disclose under rule 10b-5, can develop if the offeror, prior to making a tender offer, has made a series of market purchases and has obtained publicly undisclosed material data about the target company from target management. Fleischer & Mundheim, *supra* note 9, at 332. Offerors obtain this inside information relatively infrequently, however. *Id.* at 331.

14. Act of July 29, 1968, Pub. L. No. 90-439, 82 Stat. 454.

full and fair disclosure for the benefit of investors while at the same time providing the offeror and management equal opportunity to fairly present their case."¹⁵

The five elements of an action under section 14(e) of the Williams Act¹⁶ parallel the five elements of the common law tort of deceit.¹⁷ The plaintiff must prove that target management made, in connection with a tender offer: (1) a misstatement or omission;¹⁸ (2) of a material fact;¹⁹ (3) with intent to

15. S. REP., *supra* note 1, at 3.

16. Section 14(e) provides in full:

It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation. The Commission shall, for the purposes of this subsection, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative.

Twenty-seven states have enacted statutes that parallel section 14(e) and outlaw fraudulent conduct either in connection with a takeover bid or in connection with a tender offer. ALASKA STAT. § 45.57.040 (1980); ARK. STAT. ANN. § 67-1264.4 (1980); COLO. REV. STAT. § 11-51-123 (Supp. 1981); CONN. GEN. STAT. ANN. § 36-462 (West 1981); GA. CODE ANN. § 22-1905 (1977); Illinois Business Take-Over Act, § 8, ILL. ANN. STAT. ch. 121 1/2, § 137.58 (Smith-Hurd Supp. 1981); IND. CODE ANN. § 23-2-3.1-8.5 (Burns Supp. 1981); LA. REV. STAT. ANN. § 51:1503 (West Supp. 1982); ME. REV. STAT. ANN. tit. 13, § 808 (1981); MD. CORPS. & ASS'NS CODE ANN. § 11-904 (Supp. 1981); MASS ANN. LAWS ch. 110C, § 7 (Michie/Law. Coop. Supp. 1981); MICH. COMP. LAWS ANN. § 451.910 (Supp. 1981); MINN. STAT. § 80B.05 (1980); MISS. CODE ANN. § 75-72-109 (Supp. 1981); MO. ANN. STAT. § 409.525 (Vernon 1979); NEB. REV. STAT. § 21-2412 (1977); NEV. REV. STAT. § 78.3777 (1973); N.H. REV. STAT. ANN. § 421-A:8 (Supp. 1979); N.J. STAT. ANN. § 49:5-8 (West Supp. 1981); N.Y. BUS. CORP. LAW § 1611 (McKinney Supp. 1981); N.C. GEN. STAT. § 78B-5 (1981); OKLA. STAT. ANN. tit. 71, § 442 (West 1981); S.D. CODIFIED LAWS ANN. § 47-32-11 (Supp. 1981); TENN. CODE ANN. § 48-2106 (1979); UTAH CODE ANN. § 61-4-7 (1978); VA. CODE § 13-1-533 (1978); WIS. STAT. § 552.09 (1977). See also FED. SEC. CODE § 1602(a)(3) (Proposed Official Draft 1978) (statute patterned on section 14(e)).

17. A plaintiff must prove the following elements to state a cause of action for deceit: a false representation made by the defendant; knowledge or belief on the part of the defendant that the representation is false, or the defendant's lack of a sufficient basis of information to make the representation (the scienter requirement); the defendant's intention to induce the plaintiff to act or refrain from acting in reliance on the misrepresentation; justifiable reliance by the plaintiff in acting or refraining from action; and damage to the plaintiff due to such reliance. W. PROSSER, HANDBOOK OF THE LAW OF TORTS § 105, at 685-86 (4th ed. 1971).

18. *Chris-Craft Indus. v. Piper Aircraft Corp.*, 480 F.2d 341, 362 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973).

19. In proving materiality, a plaintiff must demonstrate that reasonable persons would consider a particular fact important in making an investment decision. *Id.* at 363.

defraud third party investors;²⁰ (4) who subsequently relied on the misrepresentations or omissions;²¹ and (5) suffered damage as a result of that reliance.²²

III. IMPLIED CAUSES OF ACTION UNDER SECTION 14(e) ON BEHALF OF TARGET SHAREHOLDERS

Only the SEC has explicit authority to act under section 14(e).²³ In recognizing section 14(e) suits by target company

20. Courts have used two different standards in determining the culpability of defendants under section 14(e). Some courts advocate a negligence standard. *See, e.g., SEC v. Wills*, 472 F. Supp. 1250, 1268 (D.D.C. 1978). Other courts support a standard of reckless failure to make available material facts that the defendant could have discovered with reasonable effort. *See, e.g., Chris-Craft Indus. v. Piper Aircraft Corp.*, 480 F.2d 341, 363-64 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973).

The Supreme Court recently held in *Aaron v. SEC*, 446 U.S. 680 (1980), that plaintiffs need not prove scienter under either section 17(a)(2) or section 17(a)(3) of the Securities Act of 1933 but must do so under section 17(a)(1). *Id.* at 697. Section 17(a)(1) makes it unlawful "to employ any device, scheme, or artifice to defraud." The Court noted that this language indicates that intent is an element. *Id.* It reasoned, however, that section 17(a)(2), which prohibits the procurement of money or property "by means of any untrue statement of a material fact or any omission to state a material fact," does not imply that a plaintiff must prove intent to defraud. *Id.*

Section 14(e) has two operative portions. The first provision makes it unlawful "to make any untrue statement of a material fact or to omit to state any material fact." This language is similar to section 17(a)(2), and thus plaintiffs alleging a violation under this portion of the statute should arguably not have to prove scienter. *But see Adams v. Standing Knitting Mills*, 623 F.2d 422, 431 (6th Cir.), *cert. denied sub nom. Adams v. Peat, Marwick, Mitchell & Co.*, 449 U.S. 1067 (1980) (ignoring the first clause of section 14(e)); *SEC v. Texas Int'l Co.*, 498 F. Supp. 1231, 1252 (N.D. Ill. 1980) (same).

The second provision of section 14(e) makes it unlawful "to engage in any fraudulent, deceptive, or manipulative acts or practices." This language, like section 17(a)(1), implies that a plaintiff must prove intent to deceive. Plaintiffs alleging a section 14(e) violation on these grounds should, therefore, arguably have to prove scienter. *See Note, Tender Offer Developments in 1980*, 38 WASH. & LEE L. REV. 999, 1005 (1981).

21. *Chris-Craft Indus. v. Piper Aircraft Corp.*, 480 F.2d 341, 373 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973).

22. Section 28(a) of the 1934 Act provides that "no person permitted to maintain a suit for damages . . . shall recover . . . a total amount in excess of his actual damages." 15 U.S.C. § 78b(a) (1976). In *Osofsky v. Zipf*, 645 F.2d 107 (2d Cir. 1981), the court concluded that "actual damages" refers to compensatory damages under a "benefit-of-the-bargain" standard rather than an "out-of-pocket" loss standard if the court can readily calculate such damages. *Id.* at 114. *See also Panther v. Marshall Field & Co.*, 646 F.2d 271, 283 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981).

23. As originally enacted, section 14(e) did not explicitly grant the SEC rulemaking powers. Congress amended the statute in 1970 to give the SEC express authority to promulgate regulations proscribing fraudulent conduct. Act of Dec. 22, 1970, Pub. L. No. 91-567, § 5, 84 Stat. 1497, 1498. Although the SEC has enacted a variety of regulations, it has used its enforcement powers to institute lawsuits under section 14(e) on only eight occasions. *SEC v. Mize*, 615 F.2d

shareholders, the courts must, therefore, imply a cause of action. The initial barrier facing a court that wishes to do so is the Supreme Court's current unsympathetic attitude toward implied causes of action.

A. THE SUPREME COURT'S RELUCTANCE TO IMPLY PRIVATE CAUSES OF ACTION

The Supreme Court was once very willing to imply private causes of action under federal statutes.²⁴ *Cort v. Ash*,²⁵ however, marked a shift in the Supreme Court's approach to implied causes of action. The Court set out a more stringent, four-factor test for implying causes of action. The Court asked whether the plaintiff belonged to "the class for whose *especial* benefit" Congress enacted the statute, whether there was any evidence that the legislature intended to create a private remedy, whether a private remedy was consistent with the legislative scheme of the statute, and whether the cause of action was one traditionally relegated to state law.²⁶ When lower courts began to use these factors freely to justify implying causes of

1046 (5th Cir.), *cert. denied*, 449 U.S. 901 (1980); SEC v. Banca Della Svizzera Italiana, [1981-1982 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 98,346 (S.D.N.Y. Nov. 16, 1981); SEC v. Texas Int'l Co., 498 F. Supp. 1231 (N.D. Ill. 1980); Wellman v. Dickinson, 475 F. Supp. 783 (S.D.N.Y. 1979); SEC v. Wills, 472 F. Supp. 1250 (D.D.C. 1978); SEC v. General Host Corp., 438 F. Supp. 105 (S.D.N.Y. 1977); SEC v. American Beef Packers, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,079 (D. Neb. May 4, 1977); SEC v. Milgo Elec. Corp., No. 77-0189 (D.D.C. Feb. 3, 1977) (available Feb. 28, 1982 on LEXIS, Fedsec library, Courts file). In comparison, the federal reporters reveal that private parties have sought relief under section 14(e) on over 300 occasions. The SEC has, however, recently authorized its General Counsel to determine whether to submit briefs, *amicus curiae*, urging equitable relief in cases arising under the Williams Act. SEC Litigation Release No. 9625, Mar. 23, 1982, *reprinted in* [1982 Current Binder] FED. SEC. L. REP. (CCH) ¶ 83,200, at 84,950.

24. *See, e.g.*, J.I. Case Co. v. Borak, 377 U.S. 426 (1964) (Court implied a private damage action under section 14(a) of the 1934 Act, 15 U.S.C. § 78n(a) (1976)). The majority relied upon the statutory language indicating that Congress enacted section 14(a) "for the protection of investors." *Id.* at 432 (quoting 15 U.S.C. § 78n(a) (1976)). According to the Court, this purpose "impl[ie]d the availability of judicial relief where necessary to achieve that result." *Id.*

Section 14(a) makes it

unlawful for any person . . . to solicit or to permit the use of his name to solicit any proxy or consent or authorization in respect of any security . . . in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78n(a) (1976).

25. 422 U.S. 66 (1975).

26. *Id.* at 78. The majority applied this four-tiered analysis and denied the plaintiff a private right of action under a federal criminal statute prohibiting corporate contributions to presidential election campaigns. *Id.* at 80-85.

action,²⁷ the Supreme Court retreated even further.²⁸ In *Cannon v. University of Chicago*,²⁹ although a majority of the Court inferred a private cause of action under the Education Amendments Act of 1972,³⁰ Justice Rehnquist, in his concurring opinion, adopted a fairly narrow interpretation of *Cort*, emphasizing its second factor, which focuses on legislative intent.³¹ In his dissent, Justice Powell openly attacked the *Cort* analysis, and urged that the Court imply private relief only on the basis of "the most compelling evidence" that Congress intended such relief.³²

The Court appeared to follow these critical views in *Touche Ross & Co. v. Redington*,³³ in which the majority refused to in-

27. Justice Powell noted in 1979 that since *Cort v. Ash*, at least twenty appellate decisions had applied the *Cort* standard to imply federal private causes of action. *Cannon v. University of Chicago*, 441 U.S. 677, 741-42 (1979) (Powell, J., dissenting). See, e.g., *Montgomery Improvement Ass'n v. HUD*, 645 F.2d 291, 295 (5th Cir. 1981) (court implied injunctive relief for city residents under title VI of the 1964 Civil Rights Act and the Housing & Community Development Act of 1974); *Wachovia Bank & Trust v. National Student Mktg. Corp.*, 650 F.2d 342, 351-53 (D.C. Cir. 1980), *cert. denied sub nom. White & Case v. Wachovia Bank & Trust Co.*, 452 U.S. 954 (1981) (court implied damage relief to buyers of newly issued securities under section 10(b) of the 1934 Act; *Chumney v. Nixon*, 615 F.2d 389, 394 (6th Cir. 1980) (court implied damage action under criminal statute of the Federal Aviation Act of 1958 providing penalties for personal assaults on aircraft within United States special aircraft jurisdiction).

28. *J.I. Case Co. v. Borak*, 377 U.S. 426 (1964), represents the Supreme Court's most liberal approach. After *Cort*, the Supreme Court heard, and rejected, a variety of different pleas for implying private remedies in federal statutes lacking an explicit private remedy. See *California v. Sierra Club*, 451 U.S. 287 (1981) (refused to imply private injunctive relief under section 10 of the Rivers and Harbors Appropriation Act of 1899); *Universities Research Ass'n v. Coutu*, 450 U.S. 754 (1981) (rejected an employee's claim for back wages as an implied right of action under the Davis-Bacon Act); *Transamerica Mortgage Advisors v. Lewis*, 444 U.S. 11 (1979) (rejected an implied damage claim under section 206 of the Investment Advisers Act of 1940, 15 U.S.C. § 80b-6 (1976)); *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979) (denied private damage action under section 17(a) of the 1934 Act); *Piper v. Chris-Craft Indus.*, 430 U.S. 1 (1977) (denied defeated tender offeror implied damage relief against target company under section 14(e) of the Williams Act).

29. 441 U.S. 677 (1979).

30. *Id.* at 689-708 (construing 20 U.S.C. § 1681(a) (1976)). The plaintiff claimed, under section 901(a) of title IX of that act, that a medical school was guilty of sex discrimination in denying her application for admission. 441 U.S. at 680.

31. Justice Rehnquist stated that "[t]he question of the existence of a private right . . . is basically one of statutory construction . . . [which depends upon] an intent to create a private right of action." 441 U.S. at 717-18 (Rehnquist, J., concurring).

32. *Id.* at 749 (Powell, J., dissenting). Justice Powell thought that *Borak* was an anomaly. *Id.* at 735-36.

33. 442 U.S. 560 (1979). Justice Powell did not take part in the *Redington* decision.

fer a private remedy under section 17(a) of the 1934 Act.³⁴ Like Justices Powell and Rehnquist in *Cannon*, the Court stressed the importance of congressional intent,³⁵ and concluded that Congress did not intend to create a private cause of action under section 17(a), reasoning that the section has no remedies for its violation and is thus not proscriptive in character.³⁶ The Court also argued that if Congress had intended to provide a private remedy in section 17(a), it could have done so, just as it did in sections 9(a), 16(b), and 18(a) of the same Act.³⁷ Finally, it pointed out that section 18(a), which provided a private remedy for the alleged wrong, did not extend that remedy to the plaintiff, and refused to expand Congress's express language.³⁸

The Supreme Court confirmed its antipathy toward implied causes of action in *Transamerica Mortgage Advisors v. Lewis*,³⁹ refusing to imply damage relief under section 206 of the Investment Advisers Act of 1940,⁴⁰ a broad antifraud provision. The Court concluded that Congress intended to exclude private litigation for damages under the statute.⁴¹ Although the section was proscriptive and intended to benefit the plaintiff,⁴² the Court argued that Congress was aware that it could have granted private relief under section 206, since it provided for such relief in other independent sections of the Act,⁴³ and refused to expand the relief that Congress had chosen to give.⁴⁴ The Court has continued to emphasize congressional intent

34. 15 U.S.C. § 78q(a) (1976). Section 17(a) is a reporting requirement for national securities exchanges, members of national securities exchanges, and brokers and dealers who transact securities business through such members.

35. 442 U.S. at 575. The majority argued that even the *Cort* majority had stressed the importance of legislative intent. "Indeed, the first three factors discussed in *Cort* . . . are ones traditionally relied upon in determining legislative intent." *Id.* at 575-76.

36. *Id.* at 568-71.

37. *Id.* at 571-72.

38. *Id.* at 572-74. Section 18(a) provides a private remedy for misstatements contained in the reports required under section 17(a) that is available only to purchasers and sellers of securities. 15 U.S.C. § 78r(a) (1976). The Court refused to extend this remedy to the plaintiff, who was neither a purchaser nor a seller. *Id.* at 574.

39. 444 U.S. 11 (1979).

40. 15 U.S.C. § 80b-6 (1976).

41. 444 U.S. at 24.

42. *Id.* at 16.

43. *Id.* at 20-21.

44. *Id.* at 20. Under the statute at issue in *Transamerica*, however, unlike that at issue in *Redington*, there were no private remedies, only administrative and criminal sanctions. *Id.* The majority also argued that Congress's omission of the phrase "actions at law" from the Act's jurisdictional component meant that Congress intended no damage relief under the Act. *Id.* at 22.

and to refuse to infer private causes of action.⁴⁵

Despite the Supreme Court's skepticism of implied rights of action,⁴⁶ it has not totally foreclosed the implication of private remedies. The Court, for example, held that private injunctive relief was an available remedy in *Transamerica*,⁴⁷ even though it refused to grant private damage relief in the same case.⁴⁸ According to the Court in both *Transamerica*⁴⁹ and *Redington*,⁵⁰ it is willing to infer private relief if the plaintiff demonstrates that Congress intended to grant this remedy. The Court has indicated that plaintiffs can demonstrate this intent

45. See, e.g., *California v. Sierra Club*, 451 U.S. 287, 293 (1981); *Universities Research Ass'n v. Coutu*, 450 U.S. 754, 770 (1981). If the plaintiff does not demonstrate congressional intent, the other *Cort* factors are irrelevant. In *Transamerica*, for example, the plaintiff argued that, despite congressional intent, the Court should imply private relief, because such relief was consistent with the statute and was not traditionally relegated to state law. 444 U.S. at 23. The majority rejected the plaintiff's arguments, stating that these two *Cort* factors "standing alone" would not justify the implication of a private remedy. *Id.* at 23-24. The Supreme Court, however, has not overruled *Cort*. Justice Powell, the most severe critic of *Cort*, recently implied that *Cort v. Ash* was still viable. See *Arguments Before the Court—Securities and Exchanges: Commodities; implied rights of action*, 50 U.S.L.W. 3411, 3412 (1981).

46. Many commentators interpret *Redington* and *Transamerica* as signaling the Supreme Court's stricter approach to implication of private relief. See, e.g., Frankel, *Implied Rights of Action*, 67 VA. L. REV. 553, 562 (1981); Underwood, *Transamerica Mortgage Advisors, Inc. v. Lewis: An Analysis of the Supreme Court's Definition of an Implied Right of Action*, 7 PEPPERDINE L. REV. 533, 548 (1980); Note, *Implied Causes of Action: A Product of Statutory Construction or the Federal Common Law Powers?*, 51 U. COLO. L. REV. 355, 355 (1980); Note, *The Federal Securities Acts: The Demise of the Implied Private Rights Doctrine?*, 1980 U. ILL. L.F. 627, 630; Note, *Private Causes of Action from Federal Statutes: A Strict Standard for Implication by Sole Reliance on Legislative Intent*, 14 U. RICH. L. REV. 605, 618-19 (1979).

The Court has limited private remedies in securities cases ten times since 1975. *Transamerica Mortgage Advisors v. Lewis*, 444 U.S. 11 (1979); *Touche Ross & Co. v. Redington*, 442 U.S. 560 (1979); *International Bhd. of Teamsters v. Daniel*, 439 U.S. 551 (1979); *Santa Fe Indus. v. Green*, 430 U.S. 462 (1977); *Piper v. Chris-Craft Indus.*, 430 U.S. 1 (1977); *TSC Indus. v. Northway, Inc.*, 426 U.S. 438 (1976); *Radzanower v. Touche Ross & Co.*, 426 U.S. 148 (1976); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976); *Rondeau v. Mosinee Paper Corp.*, 422 U.S. 49 (1975); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975). One commentator, noting the Court's extensive activity in this area, stated that "[t]here can be little doubt about the intensity of the Court's concern over the expansion of securities liability, and its determination to curb [this trend]." 4 A. BROMBERG, *SECURITIES LAW, FRAUD, SEC RULE 10B-5* at § 384.2 (1977). As this issue of the *Minnesota Law Review* went to press, however, the Supreme Court issued a new and more liberal standard for the implication of private relief in federal statutes. *Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 50 U.S.L.W. 4457, 4464 (1982). See *infra* note 85.

47. 444 U.S. at 19.

48. See *supra* text accompanying note 40.

49. See 444 U.S. at 18-19.

50. See 442 U.S. at 575-76.

by meeting the four *Cort* factors.⁵¹

The Court specifically addressed the availability of implied causes of action under section 14(e) in *Piper v. Chris-Craft Industries*,⁵² and refused to imply a cause of action for the plaintiff,⁵³ a defeated tender offeror. Although this decision appears to confirm the Court's general skepticism of implied private relief, the Court focused on the role of the plaintiff as a tender offeror.⁵⁴ The Court used the four *Cort* factors to buttress its conclusion that Congress intended the Williams Act neither to protect such offerors,⁵⁵ nor to give this class a cause of action for damages.⁵⁶ In contrast, the Court asserted that target company shareholders are "the *direct* and *intended* beneficiaries of the legislation."⁵⁷ Although the Court explicitly declined to rule whether target shareholders could raise claims under section 14(e),⁵⁸ its analysis clearly does not preclude, and may support, such a cause of action. Thus, if one demonstrates that section 14(e) satisfies the four *Cort* criteria, the Supreme Court might imply a cause of action for target shareholders.

B. IMPLYING SECTION 14(E) PRIVATE CAUSES OF ACTION TO PROTECT SHAREHOLDERS' TENDER OFFER DECISIONS

Lower federal courts have traditionally implied private relief for target shareholders who base their claims on the damages that they may incur or have incurred in deciding to tender their shares.⁵⁹ Target shareholders can base three distinct private causes of action on this rationale. First, they can claim relief for target management's post-tender offer misconduct that has affected their tender decision.⁶⁰ Second, they can claim damage relief for target management's pre-tender offer miscon-

51. *Cannon v. University of Chicago*, 441 U.S. at 688. For a similar indication by the Court in *Redington*, see *supra* note 35. The Court noted, however, that this would present an "atypical situation." See 441 U.S. at 717.

52. 430 U.S. 1 (1977).

53. *Id.* at 42.

54. *Id.* at 31-33.

55. *Id.* at 29-35.

56. *Id.* at 37-41.

57. *Id.* at 32. The Court strongly emphasized that Congress passed the Act to protect target shareholders. *Id.* at 28-41. It noted that the Act "was designed solely to get needed information to the investor, the constant focal point of the committee hearings." *Id.* at 31.

58. "Whether shareholder-offerees, the class protected by § 14(e), have an implied cause of action under § 14(e) is not before us, and we intimate no view on the matter." *Id.* at 42 n.28.

59. See *infra* notes 63-68 and accompanying text.

60. See *infra* text accompanying notes 63-92.

duct that has affected this same decision.⁶¹ Finally, they can claim injunctive relief before the tender offer takes effect based upon target management's pre-tender offer misconduct that may affect their future tender decisions.⁶²

1. *Post-Tender Offer Misconduct*

Most federal courts have recognized the right of target shareholders to bring an action under section 14(e) against target management for the misrepresentations that management makes after a tender offer takes effect.⁶³ These courts have implied a cause of action for target shareholders who have relied to their detriment⁶⁴ on target management's misstatements by either tendering⁶⁵ or failing to tender⁶⁶ their shares to the bidder. Under these decisions, shareholders may sue for either injunctive relief⁶⁷ or for damages.⁶⁸ Post-tender offer misconduct that affects a shareholder's tender decision is the most compelling example of conduct for which target shareholders should be able to sue under section 14(e); such a cause of action squarely satisfies all four *Cort* criteria.

Target shareholders clearly belong to the class for whose "especial benefit" Congress passed the Williams Act. In *Piper v. Chris-Craft Industries*, the Supreme Court indicated that

61. See *infra* text accompanying notes 93-112.

62. See *infra* text accompanying notes 113-23.

63. See, e.g., cases cited *infra* notes 64, 66-68. In a shareholder's suit under section 14(e), based on the offeror's omission of information from the tender offer itself, the Seventh Circuit noted that "[a]lthough the Williams Act contains no explicit provision for a private cause of action, it is generally accepted that there is an implied right of action under § 14(e)." *Indiana Nat'l Bank v. Mobil Oil Corp.*, 578 F.2d 180, 183 n.5 (7th Cir. 1978). The Fifth Circuit followed "the overwhelming weight of authority" in implying a cause of action under section 14(e) for a target shareholder suing for misrepresentation made after the tender offer took effect. *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579, 596 n.20 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974). One court has implied a cause of action under section 14(e) even though the tender offeror withdrew the offer *after* it had taken effect. *Fabrikant v. Jacobellis*, [1969-1970 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 92,686, at 99,018 (E.D.N.Y. June 3, 1970).

64. In *Hundahl v. United Benefit Life Ins.*, 465 F. Supp. 1349 (N.D. Tex. 1979), nontendering shareholders who sued target management for damages did not succeed in stating a claim, since the shareholders admitted that target management had not fooled them into retaining their securities. *Id.* at 1369.

65. *Id.* at 1367 (dicta).

66. *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579, 596 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974); *Hundahl v. United Benefit Life Ins.*, 465 F. Supp. 1349, 1367 (N.D. Tex. 1979); *Peterson v. Federated Dev. Co.*, 387 F. Supp. 355, 359 (S.D.N.Y. 1974).

67. *Smith v. Newport Nat'l Bank*, 326 F. Supp. 874, 877 (D.R.I. 1971).

68. *Newman v. Electronic Speciality Co.*, [1969-1970 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 92,591, at 98,703 (N.D. Ill. Dec. 31, 1969).

Congress enacted section 14(e) solely for the benefit of target shareholders.⁶⁹ The legislative history of the Williams Act supports this conclusion.⁷⁰ Given this legislative history and its clear interpretation by the Supreme Court, this cause of action satisfies the first *Cort* factor.

Under the second *Cort* factor, a court must decide whether any evidence of legislative intent suggests that it should recognize private relief. Congress plainly enacted section 14(e) to protect target shareholders from making uninformed tender decisions. Although section 14(e) itself makes no reference to the protection of investors or of target shareholders, its legislative history indicates that Congress wanted to ensure that investors made fully informed investment decisions.⁷¹

69. 430 U.S. at 28-32. See *supra* note 57 and accompanying text. One commentator suggests that target shareholders not only belong to the section 14(e) protected class, but that they constitute the entire class. Pitt, *Standing to Sue Under the Williams Act After Chris-Craft: A Leaky Ship on Troubled Waters*, 34 BUS. LAW. 117, 188 (1978).

70. During the Senate hearings on the bill, Manuel F. Cohen, SEC chairman, testified that "the general approach of . . . this bill is to provide the investor, the person who is required to make a decision, an opportunity to examine and to assess the relevant facts." *Sen. Hearings, supra* note 6, at 15. When introducing his bill, S. 510, before the Senate, Senator Williams noted that "[t]his legislation will close a significant gap in investor protection under the Federal securities laws by requiring the disclosure of pertinent information to stockholders when persons seek to obtain control of a corporation by a cash tender offer or through open market or privately negotiated purchases of securities." 113 CONG. REC. 854 (1967) (statement of Sen. Williams).

The Senate and House reports noted that "[t]he public shareholder must . . . with severely limited information, decide what course of action he should take [with respect to a tender offer] . . . This is precisely the kind of dilemma which our Federal securities laws are designed to prevent." S. REP., *supra* note 1, at 2; H.R. REP., *supra* note 1, at 2-3, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2812. The *Chris-Craft* court relied heavily on legislative history in its analysis. See 430 U.S. at 26-35.

71. The co-sponsor of the Williams Act, Senator Kuchel, noted that without the legislation, shareholders would have to base their investment decisions "solely on rumor, conjecture, and a market price," and that such decisions might lead to the demise of the corporation. The proposal, stated Kuchel, would "allow all to stand on an equal footing with respect to the availability of significant facts about a tender offer" and would protect both "the investor and the public interest." 113 CONG. REC. 9,338 (1967) (statement of Sen. Kuchel). Senator Williams also emphasized the need to protect target shareholders, noting that "[a]ll shareholders should have . . . information so that they can make informed investment decisions." *Id.* at 855 (statement of Sen. Williams).

Both the Senate and House reports contained a section explaining how the Williams Act would operate, entitled "Protection of Investors." S. REP., *supra* note 1, at 3; H.R. REP., *supra* note 1, at 4, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2813. This section states that the bill "is designed to require full and fair disclosure for the benefit of investors." Moreover, the title of the Act identified it as "[a]n Act providing for full disclosure of corporate equity ownership of securities under the Securities Exchange Act of 1934." Williams Act, Pub. L. No. 90-439, 82 Stat. 454 (1968).

It is apparent that one of the "investment decisions" that the Act protects is the target shareholder's decision to tender shares.⁷² In summarizing section 14(e), the House and Senate reports on the Williams Act asserted that the section applied to "persons engaged in opposing tender offers or otherwise seeking to influence the decision of investors."⁷³ The legislative history thus demonstrates that section 14(e) is an antifraud provision for the benefit of target shareholders that allows them to make fully informed investment decisions, one of which is the tender decision itself.⁷⁴

To protect the target shareholders fully, Congress must have intended that they have the right to act under section 14(e).⁷⁵ The arguments that the Court used in both *Redington* and *Transamerica* to demonstrate the absence of such congressional intent do not apply to target shareholder actions under section 14(e). First, unlike section 17(a) in *Redington*,⁷⁶ section 14(e) proscribes fraudulent conduct and thus, by its very lan-

72. Senator Williams noted that his bill would provide the information to stockholders deciding "whether or not to accept a cash tender offer." 113 CONG. REC. 855 (1967) (statement of Sen. Williams). Testifying before the Senate Subcommittee on Securities, Manuel F. Cohen, SEC chairman, stated that the Williams Act would provide the SEC with "adequate tools to deal effectively with the various techniques that have been developed, and are continuing to be devised, to initiate or to prevent takeover bids." *Sen. Hearings, supra* note 6, at 16 (statement of Manuel F. Cohen).

73. S. REP., *supra* note 1, at 11; H.R. REP., *supra* note 1, at 11, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2821.

74. To infer that Congress intended to provide target shareholders with a cause of action under section 14(e), however, one must do more than show that Congress wished to protect target shareholders. In *Transamerica Mortgage Advisors v. Lewis*, 444 U.S. 11, 24 (1979), for example, the Court concluded that Congress intended the Investment Advisors Act of 1940 to protect the victims of the fraudulent practices it prohibited, but refused to imply damage relief for the plaintiffs because of opposing indications of congressional intent. *See id.* *See also supra* notes 41-44 and accompanying text.

75. Professors William Painter and Carlos Israels both submitted written statements to the Senate in which they expressly referred to the availability of private relief. *See infra* note 89. Commenting before the Senate on the state of the law prior to the enactment of his bill, Senator Williams also noted that defrauded shareholders "would obviously have recourse to the courts," although many shareholders with valid claims would not litigate because of the expense and time involved in such litigation. 113 CONG. REC. 855 (1967) (statement of Sen. Williams). Senator Williams must have believed that his new bill allowed defrauded shareholders to bring private causes of action under section 14(e) if they were willing to invest their money and time. This interpretation is even more convincing in light of the House report indicating that the Williams Act would cost the government "very little" to administer, a comment suggesting that Congress expected private litigants to bear responsibility for enforcing section 14(e). H.R. REP., *supra* note 1, at 7, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2817.

76. *See supra* text accompanying note 36.

guage, suggests the need for a mechanism to enforce this prescription. Second, unlike the acts discussed in *Redington*⁷⁷ and *Transamerica*,⁷⁸ the Williams Act does not contain other provisions explicitly creating private causes of action. Although section 14(e) became part of the 1934 Act, which provides explicit private causes of action for violations of some of its sections, Congress passed the Williams Act in 1968 as a separate and distinct amendment. Since it was not enacted contemporaneously with sections that provided for private relief, a court may not infer, as the *Redington* court did with respect to section 17(a), that Congress rejected a private right of action under section 14(e).⁷⁹

Finally, unlike the remedies for the violations in *Redington*⁸⁰ and *Transamerica*,⁸¹ the remedy existing for violation of 14(e) does not preclude a private remedy for target shareholders. As enacted in 1968, section 14(e) did not contain any express enforcement provisions. This strongly suggests that when it enacted section 14(e), Congress expected the courts to imply private relief as necessary to enforce the section's prohibitions against misleading statements in connection with any tender offer.⁸² Congress amended section 14(e) in 1970 by expressly giving the SEC rulemaking authority to define and to prescribe means to prevent fraudulent tender offer conduct.⁸³ Since the amendment does not discuss means of enforcement, this amendment does not necessarily imply that Congress rejected private causes of action. Moreover, Congress specifically patterned the 1970 amendment after the language of section

77. See *supra* text accompanying note 37.

78. See *supra* text accompanying note 43.

79. In *Transamerica*, the Court inferred from the authorization of private suits in previous securities laws, passed several years before the Investment Advisers Act of 1940, that Congress considered private relief in the latter Act. 444 U.S. at 20. Yet the Court in *Transamerica* also emphasized that Congress had enacted, simultaneously with the Investment Advisers Act of 1940, the Investment Company Act of 1940, which again expressly created a private cause of action. *Id.* Given the absence of securities legislation enacted contemporaneously with the Williams Act, and the number of years that have passed since the enactment of the 1934 Act, the previous securities laws providing for private relief arguably should not suggest that Congress was unwilling to grant such relief under section 14(e).

80. See *supra* note 38 and accompanying text.

81. See *supra* note 44 and accompanying text.

82. At least one commentator suggested that private litigation generally fails as a method for enforcing the securities laws. See Frankel, *supra* note 46, at 570-81. Even this commentator, however, admitted that investor compensation provides a legitimate rationale for permitting private relief. *Id.* at 581.

83. See *supra* note 23.

15(c)(2) of the 1934 Act,⁸⁴ a provision regulating securities transactions in the over-the-counter markets and under which federal courts had already implied private relief.⁸⁵

The clear purpose of the statute, its legislative history, and the inapplicability of the arguments used by the Court in *Transamerica* and *Redington* to find no congressional intent to create private causes of action demonstrate that a Williams Act cause of action satisfies the requirements of the second *Cort* factor. Congress intended to give target shareholders the right to sue under section 14(e).

The third prong of the *Cort* test, which can also aid in determining congressional intent, asks whether implying a private action under section 14(e) is consistent with the legislative scheme of the Williams Act. Although the Court generally approved of injunctive relief, the opinion in *Piper v. Chris-Craft Industries*⁸⁶ suggested that a damage action is not consistent

84. 15 U.S.C. § 78o(c)(2) (1976).

85. *Franklin Nat'l Bank v. L.B. Meadows & Co.*, 318 F. Supp. 1339, 1343 (E.D.N.Y. 1970). The Supreme Court has suggested that in evaluating legislative action courts must take into account its contemporary legal context. "In sum, it is not only appropriate but also realistic to presume that Congress was thoroughly familiar with . . . important precedents . . . and that it expected its enactment to be interpreted in conformity with them." *Cannon v. University of Chicago*, 441 U.S. 677, 699 (1979). Since Congress patterned its amendment after the language of section 15(c)(2), courts may presume that Congress knew that private relief was implied under this provision and, therefore, approved of the implication of private relief under section 14(e).

This argument is strengthened by a liberal Supreme Court ruling that was announced as this Note went to press. *Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 50 U.S.L.W. 4457 (1982). In *Curran*, the Supreme Court considered whether to imply private damage relief under antifraud provisions of the Commodity Exchange Act (CEA) after Congress in 1974 explicitly strengthened administrative remedies under the CEA. Although the Court recognized that such an implied action would not satisfy the *Cort v. Ash* test, since the Act does not specify a protected class, *id.* at 4467, the 5-4 majority inferred the damage action. Justice Stevens, writing for the Court, noted that the "key" in determining whether to imply private relief is to focus on the state of the law at the time Congress reenacts a statute. "When Congress acts in a statutory context in which an implied remedy has already been recognized by the courts, . . . the question is whether Congress intended to *preserve* the preexisting remedy." *Id.* at 4464 (emphasis added). The Court reasoned that Congress intended to "preserve" the pre-1974 implied remedies under the CEA, since Congress did not eliminate such remedies by its 1974 legislation. *Id.* at 4465. Having concluded that "the dispositive question of legislative intent" was resolved, the Court stated that the remaining *Cort* factors were irrelevant. *Id.* at 4466.

The new *Curran* test would appear to be just as applicable in analyzing the 1970 amendment to section 14(e). Congress must have intended to preserve pre-1970 implied actions under section 14(e), since Congress did not eliminate such actions in the 1970 amendment.

86. The Court quoted Judge Friendly in *Electronic Specialty Co. v. International Controls Corp.*, 409 F.2d 937, 947 (2d Cir. 1969), for the proposition that

with the scheme of the Williams Act, because it would provide little additional protection to investors, and the threat of massive damage awards might deter potentially beneficial tender offers.⁸⁷

A damage action is, however, consistent with the Williams Act goal of preventing fraudulent acts in connection with tender offers. The *Chris-Craft* majority's concern that the threat of massive damage awards might deter potentially beneficial tender offers is unfounded; the removal of the damage threat by the *Chris-Craft* decision did not cause a drastic increase in the growth rate of tender offers.⁸⁸ Moreover, written statements before the Senate Subcommittee on Securities referred to implied private causes of action for damages under the Williams Act.⁸⁹ Therefore, Congress knew of the potential for implying damage relief under section 14(e) when it enacted the provision.⁹⁰

Under the final *Cort* factor, a court must determine whether the private action is traditionally relegated to state law. If the target's misrepresentations deterred takeover bidders, a target shareholder might conceivably state a cause of action under state law for interference with prospective economic advantage.⁹¹ Yet that tort requires a showing of intent to

in tender offer contests "the time when relief can best be given" occurs during the time appropriate for preliminary injunctive relief. 430 U.S. at 42.

87. *Id.* at 39-40.

88. Pitt, *supra* note 69, at 190.

89. Professor Carlos Israel's statement noted that "a private litigant could seek similar relief [as under *Borak*] before or after the significant fact such as the acceptance of his tender of securities." *Sen. Hearings, supra* note 6, at 67. Professor William Painter referred to a private action for "injured investors" in his written statement, and also referred to relief such as that in *Borak*. *Id.* at 140. The *Chris-Craft* Court found a problem with these written comments. The Court contended that courts should accord written statements "little weight," 430 U.S. at 31 n.20 (1977), and cited its opinion in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 204 n.24 (1976), for support. In *Hochfelder*, however, the Court's concern arose because the SEC offered random statements that the legislative opponents of the bill had inserted into the written record. The Court warned that opponents overstate their case when they attempt to defeat allegedly unfavorable legislation. *Id.* In the section 14(e) context, the statements of the two professors supported the bill. Senator Williams himself recognized Professor Painter's analysis. *Sen. Hearings, supra* note 6, at 128. The Court's rationale for dismissing written comments thus does not apply to the statements of Professors Israel and Painter.

90. One commentator has also asserted that denying target shareholders a damage remedy for post-tender offer misconduct would render the Williams Act a "snare and a delusion." Pitt, *supra* note 69, at 189, (quoting Baird v. Franklin, 141 F.2d 238, 245 (2d Cir.), *cert. denied*, 323 U.S. 737 (1944)).

91. To state a cause of action for interference with prospective economic advantage, the courts require a plaintiff to demonstrate: (1) the existence of a

interfere. Since target management may violate section 14(e) by a mere negligent failure to disclose material facts,⁹² it is clear that the contemplated action, or at least an action based on the negligent acts of target management during the post-tender offer period, is not traditionally relegated to state law. In addition, nothing in the legislative history of the Williams Act indicates that target shareholders have traditionally looked to state law for either injunctive or damage relief. The *Cort* analysis thus fully supports the inference of both private injunctive and damage causes of action under section 14(e) on behalf of target shareholders for post-tender offer misconduct by target management.

2. *Damage Relief for Pre-Tender Offer Misconduct*

Federal courts have not yet decided a case in which target shareholders sued for damages under section 14(e), alleging that they relied on management's pre-tender offer misconduct in deciding whether to tender their shares.⁹³ If, however, courts are faced with this situation, they should imply private damage relief under section 14(e).

The initial question is whether section 14(e) proscribes pre-tender offer misconduct. This section arguably prohibits only post-tender offer fraudulent practices, thus making the question of who may sue for this misconduct irrelevant. The language of section 14(e), however, suggests that it was directed at both pre-tender offer and post-tender offer fraud. Section 14(e) prohibits fraudulent conduct "in connection with" tender offers. While only one court has considered this phrase as it appears in section 14(e)⁹⁴, the Supreme Court has defined

valid business relation or expectancy; (2) knowledge of the relationship or expectancy on the part of the interferer; (3) an intentional interference inducing or causing a breach or termination of the relationship or expectancy; and (4) resultant damage to the plaintiff. *See, e.g.,* Thorne v. Elmore, 79 Ill. App. 3d 333, 345, 398 N.E.2d 837, 847 (1979). If, however, target management dissuades shareholders from selling their stock, a misrepresentation action may lie, since courts now limit the reach of *Ultramares Corp. v. Touche*, 255 N.Y. 170, 174 N.E. 441 (1931). *See* *Rusch Factors v. Levin*, 284 F. Supp. 85, 91 (D.R.I. 1968); *C. MORRIS, MORRIS ON TORTS* 319-28 (2d ed. 1980).

92. For a discussion of the requisite culpability a plaintiff must prove under a private section 14(e) cause of action, see *supra* note 20.

93. The Second Circuit has intimated that courts should imply this cause of action. *See infra* note 113 and accompanying text. *Cf. SEC v. Okin*, 132 F.2d 784, 786 (2d Cir. 1943) (applying the proxy rules to letters written prior to the time solicitation of proxies took place).

94. *See O'Connor & Assoc. v. Dean Witter Reynolds, Inc.*, [1982 Current Binder] FED. SEC. L. REP. (CCH) ¶ 98,443, at 92,632 (S.D.N.Y. Jan. 19, 1982). For a discussion of the case, see *infra* note 162.

the phrase under section 10(b) of the 1934 Act, which prohibits fraudulent conduct "in connection with the sale or purchase of any security."⁹⁵ In *Superintendent of Insurance v. Bankers Life & Casualty*,⁹⁶ Justice Douglas concluded that a deceptive practice need only "touch"⁹⁷ a sale of securities to be "in connection with" such a sale.⁹⁸ By analogy, under section 14(e) a deceptive practice should only have to "touch" a tender offer to be "in connection with" such an offer. Pre-tender offer misconduct by target management "touches" a tender offer because once shareholders learn of a forthcoming tender offer, they will begin to consider their options with respect to the tender offer. Management's misrepresentations will surely affect these considerations. Similarly, once a tender offer becomes effective, the pre-tender offer misconduct will continue to influence a shareholder's thinking and may ultimately affect the shareholder's tender offer decision.⁹⁹

Other language of section 14(e) also suggests that this sec-

95. 15 U.S.C. § 78j(b) (1976).

96. 404 U.S. 6 (1971). In *Bankers Life*, the state representative of the Manhattan Life Insurance Company brought a private action against defendants who had attempted to embezzle corporate assets through a series of securities transactions. The district court dismissed the section 10(b) claim by concluding that the theft did not affect the securities transactions, 300 F. Supp. 1083 (S.D.N.Y. 1969), and the Second Circuit affirmed, 430 F.2d 355 (2d Cir. 1970). The Supreme Court, however, reversed, concluding that the transactions were "in connection with" a sale of securities. 404 U.S. at 13.

97. Most federal courts interpret the *Bankers Life* test broadly. See *Ketchum v. Green*, 557 F.2d 1022, 1026 (3d Cir. 1977); see, e.g., *Jannes v. Microwave Communications, Inc.*, 461 F.2d 525, 529 (7th Cir. 1972); *Drachman v. Harvey*, 453 F.2d 722, 736-38 (2d Cir. 1972). The Fifth Circuit, however, in *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579 (5th Cir.), cert. denied, 419 U.S. 873 (1974), suggested that the standard "be fleshed out by a cautious case-by-case approach." *Id.* at 595. A plaintiff may prove that a deceptive practice "touches" a sale if the illegal manipulation and the sale constitute part of the same fraudulent scheme. *Alley v. Miramon*, 614 F.2d 1372, 1378 n.11 (5th Cir. 1980). The Third Circuit also adopted a more narrow case-by-case approach. See *Ketchum v. Green*, 557 F.2d 1022, 1027 (3d Cir. 1977).

98. 404 U.S. at 12-13. Cf. *United States v. Naftalin*, 441 U.S. 768, 773 n.4 (1979) (construed the use of the term "in" instead of "in connection with").

99. In *Applied Digital Data Sys. v. Milgo Elec. Corp.*, 425 F. Supp. 1145 (S.D.N.Y. 1977), a federal district court implied private injunctive relief for pre-tender offer misconduct under section 14(e), using this reasoning:

Although the shareholders might not in the pre-offer period be faced with a present decision whether to exchange their stock in the target corporation, statements and actions of the target corporation and the offeror during this period clearly have the capacity to affect any future decision and should thus fall within the purview of the statute. This is especially so when, as here, the competing parties by their acts and conduct clearly indicate that in fact they deem the proposal of an exchange offer to be genuine.

Id. at 1154. The Fifth Circuit echoed this analysis in *SEC v. Mize*, 615 F.2d 1046, 1054-55 (5th Cir. 1980).

tion proscribes pre-tender offer fraudulent practices. In addition to governing conduct "in connection with" a tender offer, section 14(e) governs conduct "in connection with any solicitation of security holders in opposition to or in favor of any such offer."¹⁰⁰ At the time Congress passed the Williams Act, rule 14a-9¹⁰¹ prohibited the fraudulent solicitation of proxies. Congress knew of existing interpretations of the word "solicitation" under this rule when it included the word in section 14(e).¹⁰² Under the proxy law, letters sent to shareholders prior to formal proxy request are "solicitations" if the communicator writes "under circumstances reasonably calculated to result in the procurement, withholding, or revocation of a proxy."¹⁰³ Just as pre-proxy statements may be "solicitations" under rule 14a-9, pre-tender offer statements should be "solicitations" under section 14(e) if the circumstances indicate that a tender offer will likely be made.¹⁰⁴

The legislative history of section 14(e) also indicates that Congress intended to include pre-tender offer misconduct within its scope. The House and Senate reports on the Williams Act observed that section 14(e) "would affirm the fact that persons engaged in . . . opposing tender offers . . . are under an obligation to make full disclosure of material information to those with whom they deal."¹⁰⁵ Clearly, rejecting a proposed tender offer constitutes behavior in the class of "opposing" an offer. As one federal district court has noted, "[t]here is no apparent reason . . . why a recommendation to reject a proposed tender offer is not also a recommendation to 'reject a tender offer.'"¹⁰⁶ Thus, both the language and the leg-

100. See *supra* note 16.

101. 17 C.F.R. § 240.14a-9 (1981).

102. SEC Chairman Manuel F. Cohen informed the Senate Subcommittee on Securities that the Williams Act had a close "relationship to existing provisions of the Exchange Act regulating *solicitation* of proxies." *Sen. Hearings*, *supra* note 6, at 16 (emphasis added).

103. *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579, 600 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974). See also *Studebaker Corp. v. Gittlin*, 360 F.2d 692, 696 (2d Cir. 1966); *SEC v. Okin*, 132 F.2d 784, 786 (2d Cir. 1943).

104. In the context of an action for injunctive relief under section 14(e), one court has enjoined pre-tender offer misconduct in connection with an "overall plan" to make a tender offer. *ICM Realty v. Cabot*, [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,585, at 96,048 (S.D.N.Y. June 6, 1974).

105. S. REP., *supra* note 1, at 11; H.R. REP., *supra* note 1, at 11, *reprinted in* 1968 U.S. CODE CONG. & AD. NEWS at 2821.

106. *Lewis v. McGraw*, 495 F. Supp. 27, 30 (S.D.N.Y. 1979), *aff'd*, 619 F.2d 192 (2d Cir.), *cert. denied*, 449 U.S. 951 (1980) (quoting *Applied Digital Data Sys. v. Milgo Elec. Corp.*, 425 F. Supp. 1145, 1153 (S.D.N.Y. 1977)).

islative history indicate that section 14(e) proscribes pre-tender offer fraudulent conduct.

Before implying private damage relief for this misconduct, however, a court must determine that Congress intended to create a cause of action for target shareholders who relied on this misconduct in making their tender offer decisions. As previously indicated,¹⁰⁷ federal courts should and do use the four *Cort* factors to imply private damage relief for target shareholders if the post-tender offer misrepresentations of target management adversely affect their tender decisions. There is very little difference between implying damage relief for investors who, after facing a tender offer, sue for post-tender offer misconduct and implying damage relief for investors who, after facing a tender offer, sue for pre-tender offer misconduct. The applicability of the four *Cort* factors does not change: the plaintiffs are still members of the especial class;¹⁰⁸ all the indicators of congressional intent, which suggest that section 14(e) includes a private cause of action to protect shareholders' tender decisions, are unaffected;¹⁰⁹ a damage action in the context of pre-tender offer misconduct is as consistent with the scheme of the Act as a damage action in the context of post-tender offer misconduct;¹¹⁰ and the action is not typically relegated to state law.¹¹¹

This analysis, equating the two actions, is reasonable. Both sets of investors seek compensation for the adverse effect that target management's fraud had upon their decisions to tender their shares. The only difference between the two causes of action is the time at which the misrepresentation took place. This brief time difference should not alter the shareholder's remedies, because pre-tender offer misrepresentations, like post-tender offer misrepresentations, can cause one of the harms that Congress designed section 14(e) to prevent—a

107. See *supra* text accompanying notes 63-92.

108. See *supra* text accompanying notes 69-70.

109. The goal of section 14(e), to insure that a shareholder may make a fully informed investment decision, see *supra* notes 71-73 and accompanying text, clearly remains. The comments of the section's proponents, see *supra* note 75, are not limited to actions based on post-tender offer misconduct. And the responses to the three arguments used in *Redington* and *Transamerica*, see *supra* text accompanying notes 76-85, also apply to actions based on both pre-tender offer and post-tender offer fraudulent conduct.

110. See *supra* text accompanying notes 86-90.

111. Target management can be as negligent in pre-tender offer conduct as in post-tender offer misconduct, making state law ineffective. See *supra* text accompanying notes 91-92.

shareholder's uninformed tender offer decision.¹¹²

3. *Injunctive Relief for Pre-Tender Offer Misconduct*

Federal courts have not yet decided a case in which target shareholders sued under section 14(e) for injunctive relief for pre-tender offer violations.¹¹³ If this Note's analysis is correct, a court should also imply a cause of action in such a case; section 14(e) covers pre-tender offer misconduct,¹¹⁴ and the shareholders seek to prevent uninformed tender decisions, one of the goals of the Williams Act.¹¹⁵ Yet, because the action is decided before the tender offer becomes effective, the tender offer may still be withdrawn. Thus, management's misconduct may never affect a shareholder's tender decision.¹¹⁶ It is equitable, however, for courts to enjoin target management's misconduct because failure to enjoin management may permit the tender offer to become effective despite management's misleading statements. The misleading statements may, however, affect an investor's later decision to tender, even though the statements were made before the tender offer was operative.¹¹⁷ To carry out the purpose of section 14(e), courts must act on the assumption that the tender offer will take effect, and thus halt the misconduct whenever it occurs.¹¹⁸

Concluding that tender offerors and target management

112. See *supra* note 99 and accompanying text. In *Lewis v. McGraw*, 619 F.2d 192 (2d Cir.), *cert. denied*, 449 U.S. 951 (1980), the Second Circuit stated that courts should imply private damage relief after a tender offer takes effect for shareholders who sue for pre-tender offer misconduct. *Id.* at 195 (dicta). The court noted that a contrary decision would permit circumvention of the securities laws by allowing target management to misrepresent its position until a tender offer took effect. This would circumvent the Williams Act's purpose of providing truthful information to shareholders confronted with a decision to tender their shares. See *supra* text accompanying notes 71-73.

113. Two circuit courts of appeals have recognized the validity of this action in dicta. See *Panther v. Marshall Field & Co.*, 646 F.2d 271, 287 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981); *Lewis v. McGraw*, 619 F.2d 192, 195 (2d Cir.), *cert. denied*, 449 U.S. 951 (1980). Courts have implied this action for other parties. See *infra* notes 120-23 and accompanying text. The SEC has recently authorized its General Counsel to submit a brief as *amicus curiae* in cases arising under the Williams Act urging that a district court has authority to order equitable relief. SEC Litigation Release No. 9625, Mar. 23, 1982, *reprinted in* [1982 Current Binder] FED. SEC. L. REP. (CCH) ¶ 83,200, at 84,950.

114. See *supra* text accompanying notes 94-106.

115. See *supra* notes 71-73 and accompanying text.

116. For a discussion of whether it is necessary for the action to be based on the tender decision, see *infra* notes 124-72.

117. See *supra* note 99 and accompanying text.

118. See *supra* note 112 and accompanying text. The Sixth Circuit has recognized that "[a] preliminary injunction against manipulative practices would be the only means of preserving the free, informed choice of shareholders that

can best uncover potential misrepresentations,¹¹⁹ federal courts have permitted these parties to sue for injunctive relief under section 14(e) for misleading pre-tender offer misconduct.¹²⁰ It logically follows, therefore, that target shareholders, the intended beneficiaries of the Williams Act,¹²¹ should have an implied right of action for injunctive relief¹²² if they can demonstrate that misleading pre-tender offer statements have the probable potential to harm their later tender decisions.¹²³

C. IMPLYING SECTION 14(E) PRIVATE CAUSES OF ACTION FOR DAMAGES TO PROTECT SHAREHOLDER'S NON-TENDER OFFER DECISIONS

This Note has demonstrated that section 14(e) proscribes pre-tender offer fraudulent practices.¹²⁴ The problem lies in determining the harms that Congress sought to alleviate when it forbade such conduct. As discussed above, Congress prohib-

the Williams Act was designed to protect." *Mobil Corp. v. Marathon Oil Co.*, 669 F.2d 366, 371 (6th Cir. 1981). See also *supra* note 86.

119. The Sixth Circuit has stated:

In a tender offer battle, events occur with explosive speed and require immediate response by a party seeking to enjoin the unlawful conduct. Issues such as incomplete disclosure and manipulative practices can only be effectively spotted and argued by parties with complete knowledge of the target, its business, and others in the industry. The tender offeror has frequently made intensive investigations before deciding to commence its offer and may often be the only party with enough knowledge and awareness to identify nondisclosure or manipulative practices in time to obtain a preliminary injunction.

Mobil Corp. v. Marathon Oil Co., 669 F.2d 366, 371 (6th Cir. 1981).

120. Target management was allowed to sue in *ICM Realty v. Cabot*, [1973-1974 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 94,585 at 96,048 (S.D.N.Y. June 6, 1974). Courts allowed tender offerors to sue for injunctive relief in *Applied Digital Data Sys. v. Milgo Elec. Corp.*, 425 F. Supp. 1145, 1155 (S.D.N.Y. 1977); *Royal Indus. v. Monogram Indus.*, [1976-1977 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 95,863, at 91,138 (C.D. Cal. Nov. 29, 1976); and *Crane Co. v. Anaconda Co.*, 411 F. Supp. 1208, 1209 (S.D.N.Y. 1975).

121. See *supra* notes 69-73 and accompanying text.

122. The court in *Lewis v. McGraw* stated that "[i]njunctive relief . . . may be available to restrain or correct misleading statements made by target management during the period preceding a tender offer where it appears that such an offer is likely, and that reliance upon the statements at issue is probable under the circumstances." 619 F.2d 192, 195 (2d Cir.) (dicta), *cert. denied*, 449 U.S. 951 (1980).

123. Federal courts grant preliminary injunctions on one of two grounds. Courts may grant relief if plaintiffs demonstrate probable success on the merits and possible irreparable damage if the injunction fails to issue. *Sonesta Int'l Hotels Corp. v. Wellington Assoc.*, 483 F.2d 247, 250 (2d Cir. 1973). Courts may also provide injunctive relief if plaintiffs demonstrate that there are serious questions concerning the merits making their claims fair grounds for litigation, and the balance of hardships tip decidedly toward the parties requesting the preliminary relief. *Gulf & Western Indus. v. Great Atl. & Pac. Tea Co.*, 476 F.2d 687, 692-93 (2d Cir. 1973).

124. See *supra* text accompanying notes 94-106.

ited pre-tender offer misconduct in part to ensure that target shareholders will not make misinformed tender offer decisions.¹²⁵ It is arguable that Congress also prohibited such conduct to ensure that target shareholders will not make misinformed decisions concerning whether to sell their shares in the market before a tender offer takes effect.¹²⁶ Two courts have expressly considered whether to imply a cause of action for shareholders whose claims rest on their pre-tender offer decisions not to sell their shares on the open market. In *Berman v. Gerber Products*,¹²⁷ a federal district court recognized this cause of action, although its analysis was brief.¹²⁸ In *Panter v. Marshall Field & Co.*, the Seventh Circuit held that it would not imply a remedy for shareholders who sue on these grounds.¹²⁹

In *Panter*, the offeror, Carter Hawley Hale (CHH), withdrew its tender offer for the shares of the target company, Marshall Field, before the tender offer took effect.¹³⁰ Marshall Field shareholders asserted that Marshall Field had made misrepresentations during the pre-tender offer period and sued under section 14(e), predicated their damage action on two grounds. The court dismissed the first claim, that Marshall Field's misrepresentation had caused them to lose the opportunity to tender their shares to CHH,¹³¹ holding that the plaintiffs did

125. See *supra* text accompanying notes 107-12.

126. The Supreme Court's suggestion in *Piper v. Chris-Craft Indus.*, 430 U.S. 1, 35 (1977), that the Williams Act solely protects investors facing a tender offer, does not preclude this cause of action. Read in context, Chief Justice Burger's opinion simply made a broad distinction between takeover bidders regulated by the Act and shareholders who, as public investors, gain the protection of the disclosure and antifraud provisions. *Wellman v. Dickinson*, 475 F. Supp. 783, 817 (S.D.N.Y. 1979).

127. 454 F. Supp. 1310 (W.D. Mich. 1978).

128. *Id.* at 1325.

129. 646 F.2d 271, 285-87 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981).

130. CHH, the parent company of Neiman-Marcus department stores, made a public proposal to exchange CHH stock and cash for Marshall Field stock. CHH filed the appropriate documents with the SEC announcing the proposed tender offer. Marshall Field responded to the proposal by issuing press releases stating the company's strong fiscal position as an independent corporation. The company also began an expansion program, including a move to open a store in a Houston shopping center already containing a Neiman-Marcus store, raising antitrust problems for CHH. In response to Marshall Field's action, CHH withdrew its proposal before it became effective, stating that "the expansion program announced by Marshall Field . . . has created sufficient doubt about Marshall Field's earning potential to make the offer no longer in the best interest of Carter Hawley Hale's shareholders." *Id.* at 281.

131. *Id.* at 283. Shareholders in a similar situation had raised this argument in a case decided just prior to *Panter*. See *Lewis v. McGraw*, 619 F.2d 192, 194 (2d Cir.), *cert. denied*, 449 U.S. 951 (1980). Both the shareholders in *Panter* and

not rely on any alleged misrepresentations because the tender offer never took place.¹³² The court also refused to imply a cause of action under section 14(e) for the second claim,¹³³ that in reliance on Marshall Field's misstatements about the strength of CHH, the plaintiffs failed to sell in the open market at the high price then available.¹³⁴ It based this holding on the

the shareholders in *Lewis* argued that the target's misconduct caused them to lose the opportunity to tender their shares to the offeror at a premium over the market price.

132. 646 F.2d at 283. The *Lewis* court had earlier rejected this argument for the same reason. 619 F.2d at 195. This holding is clearly correct. Under section 14(e), the plaintiffs must prove that they acted in reliance on the defendant's misrepresentations. See *supra* text accompanying note 21. In their lost opportunity argument, the shareholders never contended that they acted, refused to act, or made any decision based on the target's misconduct. Thus, there was no reliance by the shareholders. For a discussion of the *Lewis* case, see Note, *supra* note 20, at 1005-11.

133. 646 F.2d at 285. In contrast, the district court in *Panter* held that section 14(e) applies to conduct once a bidder has made a public announcement of an intention to make a tender offer. *Panter v. Marshall Field & Co.*, 486 F. Supp. 1168, 1188 (N.D. Ill. 1980), *aff'd*, 646 F.2d 271 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981). The district court concluded, however, that CHH's public announcement did not qualify as a public announcement of an intention to make an offer. *Id.* at 1190. CHH's proposal was subject by law to SEC approval, and subject by the proposal to the condition that large CHH shareholders dissenting to the acquisition program could redeem their shares. Since CHH neither sought SEC approval nor solicited dissensions among its large shareholders in the time after announcing its proposal, but prior to withdrawing it, the court reasoned that CHH had no intention of making a tender offer. *Id.* at 1191.

134. Prior to the public announcement by CHH of its proposal, Marshall Field's stock traded in the open market at twenty-two dollars. After the public announcement, and before CHH withdrew its proposal, Marshall Field's stock reached as high as thirty-four dollars. 646 F.2d at 279-80. After CHH withdrew its proposed exchange offer, the price of Marshall Field's stock fell to nineteen dollars, below the prepublic announcement price. *Id.* at 281.

Unlike the plaintiff's first argument, reliance is possible under this claim. Shareholders can sell or refuse to sell their shares in actual reliance upon target management's statements. Even shareholders who trade in the market and do not act in actual reliance can claim reliance based on the "fraud in the market theory." This theory, which arose in 10b-5 actions, allows plaintiffs to satisfy the reliance requirement if they prove that the defendant's conduct affected the integrity of the market price. See, e.g., *Ross v. A.H. Robbins Co.*, 607 F.2d 545, 553 (2d Cir. 1979); *Blackie v. Barrack*, 524 F.2d 891, 906 (9th Cir. 1975). The Fifth Circuit, however, has a more limited perspective. See *Shores v. Sklar*, 647 F.2d 462, 469 (5th Cir. 1981). See also Note, *The Reliance Requirement in Private Actions Under SEC Rule 10b-5*, 86 HARV. L. REV. 584, 592-96 (1975). Cf. *O'Connor & Assoc. v. Dean Witter Reynolds, Inc.*, [1982 Current Binder] FED. SEC. L. REP. (CCH) ¶ 98,443, at 92,632 (S.D.N.Y. Jan. 19, 1982) (court distinguished *Lewis v. McGraw*, 619 F.2d 192 (2d Cir.), *cert. denied*, 449 U.S. 931 (1980), and held that reliance was possible when option traders sold call options in a target company's stock just prior to the public announcement of a tender offer proposal, even though the bidder subsequently abandoned its plan). For a discussion of the *O'Connor* case, see *infra* note 162.

legislative history of the Williams Act,¹³⁵ the Act's focus on decisions that must be made under time pressure,¹³⁶ and the availability of injunctive relief for target shareholders.¹³⁷

To ascertain whether Congress intended to allow target shareholders to sue for adversely affected non-tender offer decisions, the central inquiry in implying a private cause of action,¹³⁸ a court should again apply the four *Cort* factors.¹³⁹ The target shareholders clearly belong to the class for whose special benefit Congress passed section 14(e).¹⁴⁰ The second *Cort* factor, legislative intent, does not favor this private cause of action as strongly. In refusing to imply a remedy for shareholders who claim damages resulting from their pre-tender offer decisions to sell on the open market, the *Panter* court noted that one of the Act's aims was to protect a shareholder's tender decision.¹⁴¹ There are many indications, however, that Congress intended to do more than just provide accurate information to allow shareholders to make wise decisions in considering whether to tender their shares.¹⁴²

The legislative history of section 14(e) is replete with comments noting that the section was designed to insure informed "investment decisions."¹⁴³ One of these "investment decisions"

135. 646 F.2d at 285-86. The court quoted the remarks of Senator Williams and Manuel F. Cohen.

136. *Id.* at 286. The court argued that a shareholder's pre-tender offer decision to sell on the market is not made under time pressure.

137. *Id.* at 286-87. The court also noted the general reluctance of the Supreme Court to imply causes of action under the federal securities laws. *Id.* at 286.

138. See *supra* text accompanying notes 49-50.

139. As noted above, see *supra* note 51 and accompanying text, the *Cort* factors are helpful in analyzing congressional intent.

140. See *supra* notes 69-70 and accompanying text.

141. "In the rather common situation where existing management or third parties contest a tender offer, shareholders may be exposed to a bewildering variety of conflicting appeals and arguments designed to persuade them either to accept or to reject the tender offer." 646 F.2d at 285 (113 CONG. REC. 855-56 (1967) (statement of Sen. Williams)).

The court quoted several of Mr. Cohen's statements. 646 F.2d at 286. It noted, for example, that the SEC chairman said "the bill is designed, first, to provide those who receive a tender offer with information adequate to an informed decision whether or not to accept." *Id.* at 286.

142. The quotation of Senator Williams, see *supra* note 141, does not suggest which harms Congress sought to alleviate in directing section 14(e) at "conflicting appeals and arguments." Since the "conflicting" statements might cause an erroneous pre-tender offer decision, just as they might cause an erroneous tender decision, the quotation can also be read as supporting shareholders' causes of action based on their decisions not to sell their shares in the market before the offer takes effect. The quotation of Manuel F. Cohen, see *supra* note 141, lists only one of the purposes of the Williams Act.

143. See *supra* notes 71-73 and accompanying text. Testifying before the

is the decision whether to tender one's shares, and one facet of this decision is whether to sell one's shares on the open market after the tender offer takes effect.¹⁴⁴ This latter choice is virtually identical to the choice which an investor faces in deciding whether to sell on the open market before the tender offer takes effect.¹⁴⁵ In both cases, a target shareholder confronts a market price that has risen above the normal trading price because of the tender offer or the announcement of a proposed tender offer.¹⁴⁶ In both cases, a shareholder may fail to take advantage of this increased price in reliance upon the target management's misrepresentations. And in both cases, the shareholders may suffer great financial loss because of their poor investment decisions.¹⁴⁷

The *Panter* court attempted to distinguish between these pre-tender and post-tender offer decisions on the basis of the pressures imposed on the shareholder. The court argued that

House Subcommittee on Commerce and Finance on the House version of the Williams Act, SEC chairman Manuel F. Cohen noted that the House and Senate bills have the purpose "solely to provide information to investors so that they can arrive at an informed investment decision." *Takeover Bids: Hearings on H.R. 14475 and S. 510 Before the Subcomm. on Commerce and Finance of the House Comm. on Interstate and Foreign Commerce*, 90th Cong., 2d Sess. 17 (1968) [hereinafter cited as *H.R. Hearings*].

144. The shareholder . . . may also sell his shares in the market or hold them and hope for the best. Without knowledge of who the bidder is and what he plans to do, the shareholder cannot reach an informed decision. He is forced to take a chance. For no matter what he does, he does it without adequate information to enable him to decide rationally what is the best possible course of action.

S. REP., *supra* note 1, at 2; H.R. REP., *supra* note 1, at 3, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2812.

145. Judge Cudahy stated in his *Panter* dissent that "[a] shareholder, who, in the face of a proposed tender offer elects not to sell into the market in reliance on management's misleading statements is in a position similar to that of a shareholder who elects not to tender to the bidder in reliance upon such statements." 646 F.2d at 312 (Cudahy, J., dissenting).

146. Stock prices often rise upon public announcement of a tender offer proposal. The recent tender offer acquisition by Du Pont of controlling interest in Conoco Oil provides a typical example. In early May 1981, before Dome Petroleum initially made a tender bid for Conoco stock, Conoco traded in the open market slightly under fifty dollars. By early August 1981, after Seagram, Du Pont, and Mobil had announced separate offers for Conoco stock, Conoco shares traded as high as ninety-six dollars. Smith, *The Making of the Megamerger*, FORTUNE, Sept. 7, 1981, at 61.

147. During the tender offer battle for Marshall Field & Co., before the tender offer was scheduled to take effect, investors traded 7,000,000 of the company's 9,000,000 shares. Losses after CHH withdrew its tender offer proposal were estimated to exceed \$100,000,000. N.Y. Times, Feb. 26, 1978, § F, at 15, col. 1. The *Panter* shareholder's benefit-of-the-bargain damage calculation, based on CHH's aborted attempt to take over Marshall Field & Co., exceeded \$200,000,000. *Panter v. Marshall Field & Co.*, 646 F.2d 271, 283 (7th Cir.), cert. denied, 102 S. Ct. 658 (1981).

the Williams Act applies only to situations in which the shareholders are pressured to "make a hasty, ill-considered decision to sell their shares"¹⁴⁸ to the tender offeror at some premium over the market price. Shareholders who must choose whether to sell their shares on the market before the tender offer takes effect do not face this pressure because they do not encounter a deadline, and they do not have the opportunity to sell their shares at a premium over the market price.¹⁴⁹ Thus, the court concluded that the Williams Act does not give a private remedy to these shareholders.

Both of these contentions are incorrect. First, section 14(e) does not necessarily operate only in pressure-filled situations. The court relied upon cases decided under section 14(d),¹⁵⁰ and ignored the substantive differences between that section and section 14(e). Section 14(d) contains a number of provisions that apply only if a tender offer is made.¹⁵¹ These provisions thus are effective only in cases in which there is pressure on shareholders, one component of a tender offer. In contrast, section 14(e) applies in a broader range of circumstances;¹⁵² it prohibits pre-tender offer as well as post-tender offer misconduct,¹⁵³ and is thus not restricted solely to tender offer contexts. One cannot, therefore, infer that the purposes of section 14(d) are identical to the purposes of section 14(e).

A conclusion that Congress intended section 14(e) to be effective only in cases in which shareholders face pressure does

148. 646 F.2d at 286.

149. *Id.*

150. The court cited *Kennecott Copper Corp. v. Curtiss-Wright Corp.*, 584 F.2d 1195, 1207 (2d Cir. 1978); *Wellman v. Dickinson*, 475 F. Supp. 783, 824-25 (S.D.N.Y. 1979); and *S-G Sec., Inc. v. Fuqua Inv. Co.*, 466 F. Supp. 1114, 1126-27 (D. Mass. 1978).

151. Section 14(d)(5), for example, provides that a shareholder who has tendered securities to an offeror may withdraw the securities deposited within seven days of publication or delivery to the shareholder of the tender offer. 15 U.S.C. § 78n(d)(5) (1976). Section 14(d)(1) makes it unlawful to make a tender offer "unless at the time copies of the offer . . . are first published . . . such person making the offer has filed with the Commission" a statement disclosing certain information about the tender offer. 15 U.S.C. § 78n(d)(1) (1976).

152. One of the opinions which the *Panter* court cited to support this argument noted the differences between section 14(d) and section 14(e). "Although broad and remedial interpretations of the Act may create no problems insofar as the antifraud provisions of subsection (e) of section 78n are concerned, this may not be true with regard to subsections (d)(5)-(d)(7)." *Kennecott Copper Corp. v. Curtiss-Wright Corp.*, 584 F.2d 1195, 1207 (2d Cir. 1978). *Cf. Indiana Nat'l Bank v. Mobil Oil Corp.*, 578 F.2d 180, 185 n.10 (7th Cir. 1978) ("Indeed, it is questionable whether § 14(e) has any application to the mechanics of a tender offer.").

153. *See supra* text accompanying notes 94-106.

not preclude application of section 14(e) to shareholder decisions not to sell their shares before the tender offer takes effect; in those instances, shareholders face a great deal of pressure. Contrary to the *Panter* court's assertion,¹⁵⁴ once an offeror proposes a tender offer, the price of the stock begins to rise.¹⁵⁵ Moreover, since an offeror may withdraw a tender offer at any time, causing the stock price to return to its normal level, shareholders must contend with pressures that result from this unknown deadline.¹⁵⁶ Shareholders face the uncertainty of whether to sell at the current inflated price, to wait and hope the market price continues to climb, to wait and hope the offer is made so that they may tender their shares, or to retain their shares despite the attractive offers. These pressures, combined with a target management's misrepresentations, are at least as compelling as the pressures associated with an effective tender offer. Thus even a narrow interpretation of Congress's intentions in passing section 14(e) would permit the implication of a cause of action for shareholders who make pre-tender offer decisions not to sell their shares on the market.

Legislative history reveals that Congress wished to "avoid tipping the balance of regulation . . . in favor of management."¹⁵⁷ If section 14(e) is not extended to cover shareholder pre-tender offer decisions, target corporations may freely engage in deceptive practices to defeat a proposed tender offer.

154. See *supra* text accompanying notes 148-49.

155. See *supra* notes 134, 146 and accompanying text. Donald L. Calvin, Vice President of the New York Stock Exchange, in testimony before a House subcommittee referred to the increase in the price of a stock that would result from public knowledge of a proposed tender offer. Calvin objected to the House of Representative's version of the Williams Act, which would have required an offeror to disclose confidentially to the SEC the offeror's intention to make a tender offer five days prior to making a public announcement.

If word of the impending offer becomes public, the price of the stock will rise toward the expected tender offer price. Thus, the primary inducement to stockholders—an offer to purchase their shares at an attractive price above the market—is lost, and the offeror may be forced to abandon its plans or to raise the offer to a still higher price.

H.R. Hearings, *supra* note 143, at 44.

156. The SEC has noted that,

once a tender offer proposal is publicly announced, market prices rise and public investors are confronted with an immediate investment decision: to sell shares they own into the market at the higher price being offered by arbitrageurs in response the announcement, or to retain those shares (or purchase shares) in anticipation they will be given an opportunity to tender to the bidder.

Brief of the SEC, *Amicus Curiae* at 21, *Panter v. Marshall Field & Co.*, 646 F.2d 271 (7th Cir.), cert. denied, 102 S. Ct. 658 (1981).

157. S. REP., *supra* note 1, at 3; H.R. REP., *supra* note 1, at 4, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2813.

As long as target management forces an offeror to withdraw its proposal before its effective date,¹⁵⁸ management will avoid all federal liability for its deceptive practices,¹⁵⁹ tipping the balance of regulation far in management's favor. In *Berman v. Gerber Products*,¹⁶⁰ the district court recognized that this result frustrates Congress's intent in enacting section 14(e)¹⁶¹ and noted that section 14(e) extends to protect target shareholders who do not dispose of their stock in the open market before the bidder withdraws its proposal.¹⁶²

158. The dissent in *Panter* noted:

The type of rule which the majority advocates [limiting section 14(e) liability to exclude situations where the bidder withdraws a tender offer proposal prior to the offer's effective date] is simply an invitation to make whatever claims and assertions may be expedient to force withdrawal of an offer. Management could speak without restraint knowing that once withdrawal is forced there is no Securities Act liability for deception practiced before withdrawal took place.

646 F.2d at 310 (Cudahy, J., dissenting). The SEC believes that the *Panter* ruling might lead incumbent management, faced with a hostile tender offer proposal, to make false public representations grossly overstating the value of the target's shares, causing a sharp rise in the target's stock price, and forcing the hostile bidder to abandon its proposal, because a tender offer would then be too expensive to complete. Memorandum of the SEC, *Amicus Curiae*, On Petitions for Rehearing and Suggestions for Rehearing *en banc* at 8 n.7, *Panter v. Marshall Field & Co.*, 646 F.2d 271 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981).

159. If target management suffers no liability under section 14(e) for its deception in fighting potential tender offer bidders, target management can engage in any conduct not illegal under state law. State law often provides the opportunity to sue target management for a breach in fiduciary duty on the theory that, once a plaintiff proves that a director has an interest in a transaction at issue, the director must prove that the transaction was fair and reasonable to the corporation. *Crouse-Hinds Co. v. InterNorth, Inc.*, 634 F.2d 690, 702 (2d Cir. 1980). In *Panter*, the plaintiffs alleged that the independence of several of Marshall Field's directors was questionable. 646 F.2d at 294-95. The plaintiffs thus claimed that Marshall Field's management must justify its actions with respect to CHH's tender offer proposal. The Seventh Circuit held, as a matter of law, that Marshall Field management's reasonable reliance on its antitrust counsel's advice justified all of Marshall Field's actions. *Id.* at 297. Consequently, if target management engages competent counsel, the target may, under both state and federal law, freely exercise its power to defeat a proposed tender offer.

160. 454 F. Supp. 1310 (W.D. Mich. 1978).

161. *Id.* at 1325. The court implied a right for target shareholders to sue target management for fraudulent practices leading the offeror to withdraw its proposal. *Id.* The court ultimately dismissed the plaintiff's claims, however, because the plaintiff did not prove the materiality of the omitted matter. *Id.* at 1329.

162. *Id.* at 1325. The court noted that it is "essential for the investing public at large . . . to possess knowledge of all material facts as soon as possible after the announcement [of a proposed] tender offer" so that any trading thereafter taking place would not be based on false rumors. *Id.* at 1316.

In an analogous context, the Federal District Court for the Southern District of New York also held that section 14(e) protects a target shareholder's decision to sell in the open market after the public announcement of a tender offer proposal, even if the bidder subsequently abandons its plan. O'Connor &

An analysis of the third *Cort* factor suggests that an implied cause of action for damages is consistent with the scheme of the Williams Act. If the Act was intended to protect shareholders from making erroneous investment decisions, including the decision whether to sell before the tender offer takes effect, then, to protect this design, one must prefer a damage action over injunctive relief.

Although injunctive relief would require target management to correct misrepresentations immediately, reducing the potential burden of litigation arising from shareholder losses due to target management's allegedly fraudulent statements or deeds,¹⁶³ courts must imply a damage remedy for shareholders against target management if they wish to comply with the scheme of the Williams Act. Injunctive relief alone is insufficient for three reasons. First, target shareholders probably do not have access to the information necessary to enjoin pre-tender offer misconduct. Because the events surrounding a tender offer occur so rapidly, only target management or the takeover bidder can likely recognize deceptive practices in time to gain pre-tender offer injunctive relief.¹⁶⁴ The entire premise of the Williams Act is that shareholders need complete disclosure, because investors cannot otherwise gain access to such information. If target management acts fraudulently, it certainly will not enjoin its own conduct. Only the offeror may know the actual truth, and it also may choose not to invest the time and expense necessary to enjoin target management's conduct. Injunctive relief thus becomes an empty remedy for target shareholders.

Even if target shareholders do gain access to the informa-

Assoc. v. Dean Witter Reynolds, Inc., [1982 Current Binder] FED. SEC. L. REP. (CCH) ¶ 98,443, at 92,631 (S.D.N.Y. Jan. 19, 1982). Rejecting the defense that section 14(e) did not proscribe trading on inside information of a prospective tender offer when the tender offer never takes place, Judge Lasker concluded:

[T]he alleged failure to disclose the impending announcement of the tender offer proposal worked to deny the target investor on [sic] the relevant information on which to decide whether to sell his shares in the same manner as fraudulent conduct operates when an offer has already been publicly announced

Since the insiders' sole purpose in effecting the trades . . . would have been to capitalize on the pending tender offer proposal, the alleged fraud was "in connection with a tender offer" under § 14(e) regardless of whether the offer actually became effective.

Id.

163. See *Panter v. Marshall Field & Co.*, 646 F.2d 271, 287 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981); *Electronic Speciality Co. v. International Controls Corp.*, 409 F.2d 937, 947 (2d Cir. 1979).

164. See *supra* note 119.

tion necessary to enjoin target management, courts may well refuse to grant a preliminary injunction. In *Electronic Specialty Co. v. International Controls Corp.*,¹⁶⁵ for example, the district court denied preliminary relief and held a full trial on the merits.¹⁶⁶ A damage remedy provides a necessary backup if a court denies injunctive relief.

The final concern with injunctive relief is that an injunction cannot compensate shareholders for losses they have already incurred. If a target's deceptive statements lead an offeror to withdraw its proposal, a successful injunction will only force the target management to make complete disclosure. It may not convince the potential offeror that the public would ignore the prior misrepresentations and find the renewed tender offer in the best interest of the two companies.¹⁶⁷ A tender opportunity may therefore be irretrievably lost. If this happens, the shareholders who relied on the target management's fraudulent assurances, refusing to take advantage of the increased market price that existed while the offeror still publicly intended to make a tender offer, will receive no compensation unless they can sue for damages.¹⁶⁸ Under normal circumstances, investors assume certain financial risks by placing funds in the securities market and should bear the burden of normal fluctuations in market prices.¹⁶⁹ The Williams Act, however, was passed to prevent fraudulent conduct that exposes shareholders to risks that Congress did not intend them to bear.¹⁷⁰ Thus, a damage

165. 409 F.2d 937 (2d Cir. 1979).

166. *Id.* at 943-44. For a discussion of the standards for granting a preliminary injunction, see *supra* note 123.

167. See Plaintiff's Memorandum of Law in Support of Motion for Preliminary Injunction at 15, *Applied Digital Data Sys. v. Milgo Elec. Corp.*, 425 F. Supp. 1145 (S.D.N.Y. 1977).

168. For an example of the large damages that shareholders may suffer, see *supra* note 147.

169. The protections of the Williams Act do not extend to cover open market stock purchases. See *Water & Wall Assoc. v. American Consumer Indus.*, [1973 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 93,943, at 93,759 (D.N.J. Apr. 19, 1973). When introducing the bill on the Senate floor, Senator Williams made a clear distinction between private acquisitions of stock and transactions covered by his bill:

Substantial open market or privately negotiated purchases of shares may . . . relate to shifts in control of which investors should be aware. While some people might say that this information should be filed before the securities are acquired, disclosure after the transaction avoids upsetting the free and open auction market where buyer and seller normally do not disclose the extent of their interest and avoids prematurely disclosing the terms of privately negotiated transactions.

113 CONG. REC. 856 (1967) (statement of Sen. Williams).

170. The competence and integrity of a company's management, and of the persons who seek management positions, are of vital importance to

action for losses resulting from such conduct is consistent with the scheme of the Williams Act.¹⁷¹

The analysis of the fourth *Cort* factor, whether the cause of action is traditionally relegated to state law, parallels the analysis of this factor in the context of post-tender offer damage actions; state law has no action that is comparable to section 14(e).¹⁷² Thus, considering the four *Cort* factors, and the strong

stockholders. Secrecy in this area is inconsistent with the expectations of the people who invest in the securities of publicly held corporations and impairs public confidence in securities as a medium of investment.

S. REP., *supra* note 1, at 2; H.R. REP., *supra* note 1, at 3, reprinted in 1968 U.S. CODE CONG. & AD. NEWS at 2812.

171. The Supreme Court has said that implied damage actions are not consistent with the scheme of section 14(e) if they are financially detrimental to target shareholders. *Piper v. Chris-Craft Indus.*, 430 U.S. 1, 39 (1977). One commentator has observed that under the *Chris-Craft* analysis, the Supreme Court might deny a cause of action for target shareholders unless the trial court entered judgment only against target management personally. This commentator argues that if the target company indemnified the directors, the company would suffer a loss that would ultimately be to the shareholders' detriment. *Pitt*, *supra* note 69, at 189. Yet, if only target directors were liable for their misrepresentations, the entire wealth of the directors would not make the target shareholders whole. One solution which fully compensates shareholders, and also prevents the target company from bearing the loss, would require all companies to carry liability insurance to cover potential damage judgments under section 14(e). Seventy-eight percent of United States companies already carry insurance to cover misrepresentations made by company directors. Burne, *Covering the Cost of Director Liability*, 34 INT'L MGMT. 35, 35 (1979). Companies would spread the cost of such insurance among all investors in the stock market. If the damage award against a target company exceeded the cost of insurance premiums, target shareholders would benefit financially from a damage award levied against target directors personally.

Pitt, however, may not have correctly analyzed the implications of *Chris-Craft*. Unless the market price of the target's stock falls more proportionally per share than the amount of the damage award, target shareholders will benefit financially from a damage award levied directly against the target. The market value of the target's stock arguably will not fall if the damage award does not affect the target's future dividend policy. See W. LEWELLEN, *COST OF CAPITAL* 88-89 (1969). If, for example, a target pays a damage judgment from a reserve of marketable securities, the corporation's earning potential may not change, and thus the future dividend policy might also not change. If, on the other hand, the present "forced dividend" leads the target to announce that future dividends will suffer, the market price of the stock may fall. Even if future dividends do suffer, however, investors may prefer the larger current "dividend" forced by the damage award rather than future economic gains obtained by selling stock or reinvesting dividends. J. VAN HORNE, *FINANCIAL MANAGEMENT & POLICY* 331 (5th ed. 1980). Target shareholders thus stand to benefit financially from a damage award levied directly against the target company. *But see* Frankel, *supra* note 46, at 577-78. At least one court has concluded, without going through this analysis, that a damage award levied directly against the target corporation benefits target shareholders in a manner unlike the damage award rejected in the *Chris-Craft* case. *In re Commonwealth Oil/Tesoro Petroleum Corp. Sec. Litig.*, 467 F. Supp. 227, 241 (W.D. Tex. 1979).

172. See *supra* text accompanying notes 91-92.

indications of congressional intent, a court should imply a private cause of action for target shareholders who sue for damages based on their decisions whether to sell on the market before the tender offer takes effect.

IV. TIMING OF PRE-TENDER OFFER LIABILITY

If section 14(e) is interpreted to allow imposition of liability on target management for pre-tender offer misrepresentations, whether these actions are based on a shareholder's pre-tender offer decision or on a shareholder's actual tender offer decision, it then becomes necessary to identify the stage at which courts should impose damage liability for pre-tender misrepresentations. Three alternative rules are available. At one extreme, courts might impose potential damage liability on target management at the earliest possible stage, once an offeror has taken "a substantial step or steps to commence"¹⁷³ a tender offer—the "substantial step" test. At the other extreme, courts might impose potential damage liability on target management at a very late stage, once an offeror both makes a public announcement of a proposed tender offer and indicates a definite intent to make an actual offer—the "definite intent" test. This Note does not accept either approach and, instead, proposes a rule making target management potentially liable in damages once any person makes a public announcement concerning a tender offer proposal—the "public announcement" test.

A. THE "SUBSTANTIAL STEP" TEST

The "substantial step" test is derived from rule 14e-3,¹⁷⁴ a SEC rule mandating any person obtaining material inside information concerning a tender offer to disclose such information to the public a reasonable time before personally engaging in market trading.¹⁷⁵ Under the rule, if any person has taken a substantial step or steps to commence a tender offer, those who

173. 17 C.F.R. § 240.14e-3 (1981).

174. *Id.* The SEC enacted the rule after the Supreme Court's decision in *Chiarella v. United States*, 445 U.S. 222 (1980). In *Chiarella*, an employee of a printing company hired by a tender offeror obtained inside information concerning the future tender offer and used this information for investment purposes, without disclosing his knowledge publicly. The Supreme Court held that the employee, absent a duty to speak, did not have to disclose his inside knowledge. *Id.* at 235. The Court found that the trial court had not instructed the jury on the duty, if any, that the employee owed to the offering company and its shareholders. *Id.* at 236.

175. If rule 14e-3 had existed at the time *Chiarella* obtained his inside

know of the proposed transaction are under a duty either to disclose their knowledge prior to trading or to abstain from trading.¹⁷⁶ In the present context, the "substantial step" test would impose potential damage liability for target management's misrepresentations made after the offeror has taken substantial steps to commence a tender offer.

Although the "substantial step" test imposes potential damage liability on target management at a very early stage in the tender offer process, and thus encourages responsible actions at this same early stage, this test has two disadvantages. First, the test would lead to extensive litigation over the meaning of a "substantial step." Although the SEC has published a list of activities that constitute a substantial step under rule 14e-3, it has explicitly noted that this list is not all-inclusive,¹⁷⁷ thus allowing management to debate the scope of the phrase. Second, the "substantial step" test would often be inconsistent with the scope of section 14(e). Many substantial steps in commencing a potential tender offer take place before either the target management or the offeror makes a public announcement.¹⁷⁸ If shareholders sue under section 14(e) for misrepresentations that occurred after the substantial steps were taken, but before a public announcement was made, they will likely not prevail; such misrepresentations arguably are too far removed from a tender offer context and are, therefore, not "in connection with" a tender offer, as required under the Williams Act.¹⁷⁹ Consequently, the "substantial step" test is an inade-

knowledge, the rule would have made him liable for not having disclosed this information before trading publicly.

176. The SEC published this list in connection with its promulgation of rule 14e-3:

The Commission believes that a substantial step or steps to commence a tender offer include, but are not limited to, voting on a resolution by the offering person's board of directors relating to the tender offer; the formulation of a plan or proposal to make a tender offer by the offering person or the person(s) acting on behalf of the offering person; or activities which substantially facilitate the tender offer such as: arranging financing for a tender offer; preparing or directing or authorizing the preparation of tender offer materials; or authorizing negotiations, negotiating or entering into an agreement with any person to act as a dealer manager, soliciting dealer, forwarding agent or depository in connection with the tender offer.

Sec. Act Release No. 6239, 45 Fed. Reg. 60,410, 60,413 n.33 (1980).

177. *Id.*

178. Many of the actions that constitute a substantial step under the SEC's list will necessarily occur before the announcement of a proposed tender offer. The offeror, for example, will certainly formulate the proposal and vote on it before making the proposed offer public.

179. If the tender offer has not even been publically proposed, the misrepresentations occur in circumstances under which investors buy and sell the tar-

quate test for imposing liability on target management.

B. THE "DEFINITE INTENT" TEST

The "definite intent" test¹⁸⁰ would extend potential damage liability to target management for misrepresentations made after an offeror has made a public announcement of a tender offer proposal and has indicated a clear and definite intent to carry out that offer. This rule has three disadvantages. The phrase "clear and definite intent," like the phrase "substantial step," is ambiguous and would be litigated frequently. A court might conclude that a clear and definite intent exists if the offeror has precisely defined the terms of the pending tender offer.¹⁸¹ Alternatively, a court might conclude that a clear and definite intent exists only if the offeror has bound itself to actually make a tender offer.¹⁸²

In addition to being ambiguous, the "definite intent" test would not prevent the target from making a misleading public announcement if the statement is made prior to the offeror's public announcement of the proposal. Since the potential offeror, under any interpretation of the test, would not yet have

get's stock with no knowledge of a forthcoming tender offer. Thus, the target's misconduct could be dealt with more appropriately under rule 10b-5, which prohibits fraudulent conduct "in connection with the purchase or sale of any security." 17 C.F.R. § 240.10b-5 (1981).

180. This two-part test is derived from Judge Weinfeld's opinion in *Applied Digital Data Sys. v. Milgo Elec. Corp.*, 425 F. Supp. 1145, 1154 (S.D.N.Y. 1977).

181. See, e.g., *Reserve Mgmt. v. Anchor Daily Income Fund*, 459 F. Supp. 597, 608 (S.D.N.Y. 1978). In this case, the district court refused to apply section 14(e) in the absence of a public announcement of a proposed tender offer or conduct indicating a clear and definite intent to make such an offer.

182. See, e.g., *Panther v. Marshall Field & Co.*, 486 F. Supp. 1168, 1190 (N.D. Ill. 1980), *aff'd*, 646 F.2d 271 (7th Cir.), *cert. denied*, 102 S. Ct. 658 (1981). If this test were so interpreted, very few proposed tender offerors would display the required "clear and definite intent." Typically, a tender offer always contains a series of conditions.

To minimize risk during a tender offer, the buyer can attach nearly as many conditions to consummation as he wants. A normal offer contains about six to eight standard conditions, which negate the transaction if untoward events occur, such as government intervention, suspension of trading of securities on the stock exchange, issuance by the target company of additional stock, any adverse change in its business or financial condition, or commencement of war involving the United States.

In addition to these, the buyer may tailor other conditions to suit his convenience in the deal.

Troubh, *Purchased Affection: A Primer on Cash Tender Offers*, HARV. BUS. REV. July-Aug. 1976, at 79, 81 (1976). The Senate, in its final report on the Williams Act, also noted the conditional nature of the tender offer: "The person making the offer obligates himself to purchase all or a specified portion of the tendered shares if certain specified conditions are met." S. REP., *supra* note 1, at 2.

shown a clear and definite intent to make a tender offer, the rule would not apply.¹⁸³ Finally, the "definite intent" test may not cover a situation in which a target company publicly announces a proposal to buy its own stock, when in fact that target never intends to make an offer but only intends to discourage a hostile bidder. By carefully wording an announcement of a proposed tender offer, target management might successfully, and deceptively, deter other potential bidders and yet avoid indicating a clear and definite intent to carry out the proposal.¹⁸⁴ The "definite intent" test therefore does not adequately place potential damage liability on target management for pre-tender offer misrepresentations.

C. THE "PUBLIC ANNOUNCEMENT" TEST

This Note proposes a rule that imposes potential damage liability on target management when a public announcement concerning a tender offer is first made. This test avoids the disadvantages inherent in the two preceding alternative rules.

There will be little litigation concerning the meaning of a "public announcement." This term has a generally accepted

183. This factual setting arose in *Humana, Inc. v. American Medicorp*, [1977-1978 Transfer Binder] FED. SEC. L. REP. (CCH) ¶ 96,268, at 92,823 (S.D.N.Y. Jan. 5, 1978). In *Humana*, Humana wrote privately to Medicorp indicating Humana's desire to make a tender offer for Medicorp stock. Medicorp responded by sending letters to its own shareholders, denouncing Humana's previously private proposal as illegal under the antitrust laws. Medicorp, however, did not state its reasons for opposing the proposal. *Id.* at 92,825. The district court granted Humana injunctive relief under section 14(e) to prevent Medicorp from making future omissions of material facts in any further correspondence concerning Humana's tender offer proposal. *Id.* at 92,833. If, because of Medicorp's misleading communication to its shareholders, Humana withdrew its tender offer proposal, Medicorp shareholders, predicated a damage action against Medicorp based on the "definite intent" test, would not state a cause of action; Humana never had the opportunity to demonstrate a "clear and definite intent" to make an offer prior to Medicorp's misrepresentations.

184. In *Levine v. Seilon, Inc.*, 439 F.2d 328 (2d Cir. 1971), a former preferred shareholder of the defendant corporation brought an action under section 14(e), claiming that the defendant had announced a stock exchange proposal without intending to make such an exchange, for the purpose of convincing preferred shareholders to approve previously rejected credit arrangements. The district court held that since no tender offer took place, section 14(e) did not apply. SEC Amicus Brief, *Levine v. Seilon, Inc.*, 439 F.2d 328 (2d Cir. 1971), reprinted in 85 SEC. REG. & L. REP. (BNA) E-2 (1971). The Second Circuit affirmed on other grounds, but noted that "we are not sure we would agree with the district court's rather restrictive reading of this provision." 439 F.2d at 335. Under the "definite intent" test, target management could continue to engage in such practices without fear of damage liability under section 14(e) as long as it avoided indicating a "clear and definite intent" to make an offer.

meaning in securities transactions,¹⁸⁵ creating a relatively bright-line test. The test will not, therefore, confront target management with an ambiguous standard. Moreover, unlike the "substantial step" test, the "public announcement" test will not exceed the scope of section 14(e). Misrepresentations made before the tender offer becomes effective, but after the proposed tender offer is announced, clearly fall within those practices that section 14(e) proscribes.¹⁸⁶

Unlike the "definite intent" test, the "public announcement" test would prevent the target management from making misleading public announcements concerning the tender offer before the offeror has publicly announced its proposal. The "public announcement" test would hold target management liable for its misconduct as long as its own announcement concerned a tender offer. Finally, also unlike the "definite intent" test, the "public announcement test" covers situations in which target management publicly offers to buy its own stock, but does not demonstrate a clear and definite intent. Thus, by circumventing all the disadvantages of the two other alternative rules, the "public announcement" test becomes the best choice for defining which pre-tender offer fraudulent practices are forbidden by section 14(e).

V. CONCLUSION

Despite the Supreme Court's general reluctance to imply private causes of action under the federal securities laws, a court should imply a private cause of action under section 14(e) for those whom Congress clearly intended to protect—target shareholders. The evidence of congressional intent most strongly supports a shareholder's action against target management for post-tender offer misconduct that affected the shareholder's tender offer decision. The same evidence also suggests that courts should imply both legal and equitable relief for pre-tender offer misconduct if it affected, or will affect, the shareholder's tender decision. Finally, indications of congressional intent even support a shareholder's damage action based on misconduct affecting the shareholder's decision not to sell securities on the open market before the offer became effective.

185. "Public announcement" involves the issuance of a press release. *See, e.g., Indiana Nat'l Bank v. Mobil Oil Corp.*, 578 F.2d 180, 185 (7th Cir. 1978). The term also should include deliberate leaks of information concerning a tender offer proposal. *See E. ARANOW, H. EINHORN & G. BERLSTEIN, supra* note 1, at 143-44.

186. *See supra* text accompanying notes 94-106.

By implying private relief for target shareholders under the Williams Act, courts will best carry out the intent of Congress in enacting section 14(e) to protect the investment decisions of the target shareholder.